

Sally Beauty Holdings, Inc.  
Form 10-Q  
May 01, 2019

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: MARCH 31, 2019

-OR-

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF  
1934  
Commission File No. 1-33145

SALLY BEAUTY HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

|                                                                                      |                                                    |
|--------------------------------------------------------------------------------------|----------------------------------------------------|
| Delaware<br>(State or other jurisdiction of incorporation or organization)           | 36-2257936<br>(I.R.S. Employer Identification No.) |
| 3001 Colorado Boulevard<br>Denton, Texas<br>(Address of principal executive offices) | 76210<br>(Zip Code)                                |

Registrant's telephone number, including area code: (940) 898-7500

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a 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   | Smaller reporting company |
|                         | Emerging growth company   |

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

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

As of April 26, 2019, there were 120,580,929 shares of the issuer’s common stock outstanding.

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In this Quarterly Report, references to “the Company,” “Sally Beauty,” “our company,” “we,” “our,” “ours” and “us” refer to Sally Beauty Holdings, Inc. and its consolidated subsidiaries unless otherwise indicated or the context otherwise requires.

cautionary notice regarding forward-looking statements

Statements in this Quarterly Report on Form 10-Q and in the documents incorporated by reference herein which are not purely historical facts or which depend upon future events may constitute 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, which we refer to as the Exchange Act. Words such as “anticipate,” “believe,” “estimate,” “expect,” “intend,” “plan,” “project,” “target,” “can,” “could,” “may,” “should,” “will,” “would” or similar expressions may also identify such forward-looking statements.

Readers are cautioned not to place undue reliance on forward-looking statements as such statements speak only as of the date they were made and involve risks and uncertainties that could cause actual events or results to differ materially from the events or results described in the forward-looking statements. The most important risks, uncertainties and other factors which could cause our actual results to differ from our forward-looking statements are set forth in our description of risk factors in Item 1A contained in our Annual Report on Form 10-K for the fiscal year ended September 30, 2018, which should be read in conjunction with the forward-looking statements in this report. Additional risks and uncertainties may also be discussed in this quarterly report and the other reports we file with the SEC. Forward-looking statements speak only as of the date they are made, and we do not undertake any obligation to update any forward-looking statement.

The events described in the forward-looking statements might not occur or might occur to a different extent or at a different time than we have described. As a result, our actual results may differ materially from the results contemplated by these forward-looking statements.

PART I — FINANCIAL INFORMATION

Item 1. Financial Statements.

The following condensed consolidated balance sheets as of March 31, 2019 and September 30, 2018, the condensed consolidated statements of earnings, condensed consolidated statements of comprehensive income, and the condensed statements of stockholders' deficit for the three and six months ended March 31, 2019 and 2018, and the condensed consolidated statements of cash flows for the six months ended March 31, 2019 and 2018 are those of Sally Beauty Holdings, Inc. and its subsidiaries.

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## SALLY BEAUTY HOLDINGS, INC. AND SUBSIDIARIES

## Condensed Consolidated Balance Sheets

(In thousands, except par value data)

(Unaudited)

|                                                                                                                                                                                                      | March 31,<br>2019 | September<br>30,<br>2018 |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------|--------------------------|
| <b>Assets</b>                                                                                                                                                                                        |                   |                          |
| Current assets:                                                                                                                                                                                      |                   |                          |
| Cash and cash equivalents                                                                                                                                                                            | \$89,777          | \$77,295                 |
| Trade accounts receivable, net                                                                                                                                                                       | 41,976            | 48,417                   |
| Accounts receivable, other                                                                                                                                                                           | 49,451            | 42,073                   |
| Inventory                                                                                                                                                                                            | 953,043           | 944,338                  |
| Other current assets                                                                                                                                                                                 | 39,895            | 42,960                   |
| Total current assets                                                                                                                                                                                 | 1,174,142         | 1,155,083                |
| Property and equipment, net of accumulated depreciation of \$636,099 at<br>March 31, 2019 and \$611,021 at September 30, 2018                                                                        | 297,124           | 308,357                  |
| Goodwill                                                                                                                                                                                             | 533,566           | 535,925                  |
| Intangible assets, excluding goodwill, net of accumulated amortization of<br>\$137,767 at March 31, 2019 and \$132,724 at September 30, 2018                                                         | 68,370            | 72,698                   |
| Other assets                                                                                                                                                                                         | 19,412            | 25,351                   |
| Total assets                                                                                                                                                                                         | \$2,092,614       | \$2,097,414              |
| <b>Liabilities and Stockholders' Deficit</b>                                                                                                                                                         |                   |                          |
| Current liabilities:                                                                                                                                                                                 |                   |                          |
| Current maturities of long-term debt                                                                                                                                                                 | \$5,503           | \$5,501                  |
| Accounts payable                                                                                                                                                                                     | 252,470           | 303,241                  |
| Accrued liabilities                                                                                                                                                                                  | 156,490           | 180,287                  |
| Income taxes payable                                                                                                                                                                                 | 6,280             | 2,144                    |
| Total current liabilities                                                                                                                                                                            | 420,743           | 491,173                  |
| Long-term debt                                                                                                                                                                                       | 1,708,421         | 1,768,808                |
| Other liabilities                                                                                                                                                                                    | 25,917            | 30,022                   |
| Deferred income tax liabilities, net                                                                                                                                                                 | 82,608            | 75,967                   |
| Total liabilities                                                                                                                                                                                    | 2,237,689         | 2,365,970                |
| Stockholders' deficit:                                                                                                                                                                               |                   |                          |
| Common stock, \$0.01 par value. Authorized 500,000 shares; 120,566 and<br>120,145 shares issued and 120,107 and 119,926 shares outstanding at<br>March 31, 2019 and September 30, 2018, respectively | 1,201             | 1,199                    |
| Preferred stock, \$0.01 par value. Authorized 50,000 shares; none issued                                                                                                                             | —                 | —                        |
| Additional paid-in capital                                                                                                                                                                           | 7,590             | —                        |
| Accumulated deficit                                                                                                                                                                                  | (48,312 )         | (179,764 )               |
| Accumulated other comprehensive loss, net of tax                                                                                                                                                     | (105,554 )        | (89,991 )                |

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|                                             |             |             |
|---------------------------------------------|-------------|-------------|
| Total stockholders' deficit                 | (145,075 )  | (268,556 )  |
| Total liabilities and stockholders' deficit | \$2,092,614 | \$2,097,414 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

## SALLY BEAUTY HOLDINGS, INC. AND SUBSIDIARIES

## Condensed Consolidated Statements of Earnings

(In thousands, except per share data)

(Unaudited)

|                                              | Three Months Ended |           | Six Months Ended  |             |
|----------------------------------------------|--------------------|-----------|-------------------|-------------|
|                                              | March 31,<br>2019  | 2018      | March 31,<br>2019 | 2018        |
| Net sales                                    | \$945,852          | \$975,321 | \$1,935,305       | \$1,970,286 |
| Cost of goods sold                           | 477,528            | 488,999   | 986,275           | 997,335     |
| Gross profit                                 | 468,324            | 486,322   | 949,030           | 972,951     |
| Selling, general and administrative expenses | 361,626            | 368,461   | 728,614           | 739,748     |
| Restructuring                                | (5,814 )           | 6,759     | (1,834 )          | 11,969      |
| Operating earnings                           | 112,512            | 111,102   | 222,250           | 221,234     |
| Interest expense                             | 23,821             | 25,262    | 48,310            | 49,277      |
| Earnings before provision for income taxes   | 88,691             | 85,840    | 173,940           | 171,957     |
| Provision for income taxes                   | 22,966             | 24,469    | 42,488            | 27,322      |
| Net earnings                                 | \$65,725           | \$61,371  | \$131,452         | \$144,635   |
| Earnings per share:                          |                    |           |                   |             |
| Basic                                        | \$0.55             | \$0.49    | \$1.10            | \$1.15      |
| Diluted                                      | \$0.54             | \$0.49    | \$1.09            | \$1.14      |
| Weighted average shares:                     |                    |           |                   |             |
| Basic                                        | 120,077            | 124,270   | 120,033           | 126,046     |
| Diluted                                      | 120,991            | 125,057   | 120,949           | 126,834     |

The accompanying notes are an integral part of these condensed consolidated financial statements.



## SALLY BEAUTY HOLDINGS, INC. AND SUBSIDIARIES

## Condensed Consolidated Statements of Comprehensive Income

(In thousands)

(Unaudited)

|                                               | Three Months |          | Six Months Ended |           |
|-----------------------------------------------|--------------|----------|------------------|-----------|
|                                               | Ended        |          | March 31,        |           |
|                                               | March 31,    | 2018     | 2019             | 2018      |
| Net earnings                                  | \$65,725     | \$61,371 | \$131,452        | \$144,635 |
| Other comprehensive loss:                     |              |          |                  |           |
| Foreign currency translation adjustments      | 3,040        | 10,437   | (10,425 )        | 10,182    |
| Interest rate caps, net of tax                | (2,140 )     | 2,310    | (4,970 )         | 1,507     |
| Foreign exchange contracts, net of tax        | 242          | —        | (168 )           | —         |
| Other comprehensive income (loss), net of tax | 1,142        | 12,747   | (15,563 )        | 11,689    |
| Total comprehensive income                    | \$66,867     | \$74,118 | \$115,889        | \$156,324 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

## SALLY BEAUTY HOLDINGS, INC. AND SUBSIDIARIES

## Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

|                                                                                     | Six Months Ended<br>March 31, |            |
|-------------------------------------------------------------------------------------|-------------------------------|------------|
|                                                                                     | 2019                          | 2018       |
| <b>Cash Flows from Operating Activities:</b>                                        |                               |            |
| Net earnings                                                                        | \$ 131,452                    | \$ 144,635 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: |                               |            |
| Depreciation and amortization                                                       | 53,275                        | 54,009     |
| Share-based compensation expense                                                    | 5,871                         | 5,850      |
| Amortization of deferred financing costs                                            | 1,979                         | 1,851      |
| (Gain) loss on extinguishment of debt                                               | (473 )                        | 876        |
| (Gain) loss on disposal of equipment and other property                             | (6,548 )                      | 42         |
| Deferred income taxes                                                               | 8,530                         | (29,379 )  |
| Changes in (exclusive of effects of acquisitions):                                  |                               |            |
| Trade accounts receivable                                                           | 5,950                         | (1,506 )   |
| Accounts receivable, other                                                          | (7,554 )                      | (3,990 )   |
| Inventory                                                                           | (14,213 )                     | 3,266      |
| Other current assets                                                                | 2,754                         | 3,508      |
| Other assets                                                                        | (1,293 )                      | 143        |
| Accounts payable and accrued liabilities                                            | (69,704 )                     | (12,175 )  |
| Income taxes payable                                                                | 4,150                         | (762 )     |
| Other liabilities                                                                   | (4,066 )                      | 13,082     |
| Net cash provided by operating activities                                           | 110,110                       | 179,450    |
| <b>Cash Flows from Investing Activities:</b>                                        |                               |            |
| Payments for property and equipment                                                 | (46,398 )                     | (38,693 )  |
| Proceeds from sale of property and equipment                                        | 12,010                        | 14         |
| Acquisitions, net of cash acquired                                                  | (2,848 )                      | (9,175 )   |
| Net cash used by investing activities                                               | (37,236 )                     | (47,854 )  |
| <b>Cash Flows from Financing Activities:</b>                                        |                               |            |
| Proceeds from issuance of long-term debt                                            | 242,504                       | 246,819    |
| Repayments of long-term debt                                                        | (304,157)                     | (260,142)  |
| Debt issuance costs                                                                 | —                             | (1,151 )   |
| Payments for common stock repurchased                                               | —                             | (114,699)  |
| Proceeds from exercises of stock options                                            | 1,721                         | 1,112      |
| Net cash used by financing activities                                               | (59,932 )                     | (128,061)  |
| Effect of foreign exchange rate changes on cash and cash equivalents                | (460 )                        | 762        |
| Net increase in cash and cash equivalents                                           | 12,482                        | 4,297      |
| Cash and cash equivalents, beginning of period                                      | 77,295                        | 63,759     |
| Cash and cash equivalents, end of period                                            | \$ 89,777                     | \$ 68,056  |
| <b>Supplemental Cash Flow Information:</b>                                          |                               |            |

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|                                            |          |          |
|--------------------------------------------|----------|----------|
| Interest paid                              | \$48,378 | \$46,574 |
| Income taxes paid                          | 37,518   | 45,089   |
| Capital expenditures incurred but not paid | \$3,763  | \$1,426  |

The accompanying notes are an integral part of these condensed consolidated financial statements.

## SALLY BEAUTY HOLDINGS, INC. AND SUBSIDIARIES

## Condensed Consolidated Statements of Stockholders' Deficit

(In thousands)

(Unaudited)

|                                   | Common Stock<br>Shares | Common Stock<br>Amount | Additional<br>Paid-in<br>Capital | Accumulated<br>Deficit | Treasury<br>Stock | Accumulated<br>Other<br>Comprehensive<br>Loss | Total<br>Stockholders'<br>Deficit |
|-----------------------------------|------------------------|------------------------|----------------------------------|------------------------|-------------------|-----------------------------------------------|-----------------------------------|
| Balance at September 30,<br>2018  | 119,926                | \$ 1,199               | \$ —                             | \$ (179,764 )          | \$ —              | \$ (89,991 )                                  | \$ (268,556 )                     |
| Net earnings                      | —                      | —                      | —                                | 65,727                 | —                 | —                                             | 65,727                            |
| Other comprehensive loss          | —                      | —                      | —                                | —                      | —                 | (16,705 )                                     | (16,705 )                         |
| Share-based compensation          | —                      | —                      | 3,354                            | —                      | —                 | —                                             | 3,354                             |
| Stock issued for stock<br>options | 115                    | 1                      | 1,448                            | —                      | —                 | —                                             | 1,449                             |
| Balance at December 31,<br>2018   | 120,041                | \$ 1,200               | \$ 4,802                         | \$ (114,037 )          | \$ —              | \$ (106,696 )                                 | \$ (214,731 )                     |
| Net earnings                      | —                      | —                      | —                                | 65,725                 | —                 | —                                             | 65,725                            |
| Other comprehensive income        | —                      | —                      | —                                | —                      | —                 | 1,142                                         | 1,142                             |
| Share-based compensation          | —                      | —                      | 2,517                            | —                      | —                 | —                                             | 2,517                             |
| Stock issued for stock<br>options | 66                     | 1                      | 271                              | —                      | —                 | —                                             | 272                               |
| Balance at March 31, 2019         | 120,107                | \$ 1,201               | \$ 7,590                         | \$ (48,312 )           | \$ —              | \$ (105,554 )                                 | \$ (145,075 )                     |

|                                                         | Common Stock<br>Shares | Common Stock<br>Amount | Additional<br>Paid-in<br>Capital | Accumulated<br>Deficit | Treasury<br>Stock | Accumulated<br>Other<br>Comprehensive<br>Loss | Total<br>Stockholders'<br>Deficit |
|---------------------------------------------------------|------------------------|------------------------|----------------------------------|------------------------|-------------------|-----------------------------------------------|-----------------------------------|
| Balance at September 30,<br>2017                        | 129,585                | \$ 1,296               | \$ —                             | \$ (283,076 )          | \$ —              | \$ (81,836 )                                  | \$ (363,616 )                     |
| Net earnings                                            | —                      | —                      | —                                | 83,264                 | —                 | —                                             | 83,264                            |
| Other comprehensive loss                                | —                      | —                      | —                                | —                      | —                 | (1,058 )                                      | (1,058 )                          |
| Repurchases and cancellations<br>of<br><br>common stock | (3,848 )               | (39 )                  | (3,386 )                         | (61,187 )              | —                 | —                                             | (64,612 )                         |
| Share-based compensation                                | —                      | —                      | 3,111                            | —                      | —                 | —                                             | 3,111                             |
| Stock issued for stock options                          | 62                     | 1                      | 275                              | —                      | —                 | —                                             | 276                               |
| Balance at December 31,<br>2017                         | 125,799                | \$ 1,258               | \$ —                             | \$ (260,999 )          | \$ —              | \$ (82,894 )                                  | \$ (342,635 )                     |
| Net earnings                                            | —                      | —                      | —                                | 61,371                 | —                 | —                                             | 61,371                            |
| Other comprehensive income                              | —                      | —                      | —                                | —                      | —                 | 12,747                                        | 12,747                            |

Repurchases and cancellations  
of

|                                |          |          |          |               |      |              |               |
|--------------------------------|----------|----------|----------|---------------|------|--------------|---------------|
| common stock                   | (2,899 ) | (29 )    | (3,573 ) | (46,484 )     | —    | —            | (50,086 )     |
| Share-based compensation       | —        | —        | 2,738    | —             | —    | —            | 2,738         |
| Stock issued for stock options | 102      | 1        | 835      | —             | —    | —            | 836           |
| Balance at March 31, 2018      | 123,002  | \$ 1,230 | \$ —     | \$ (246,112 ) | \$ — | \$ (70,147 ) | \$ (315,029 ) |

The accompanying notes are an integral part of these condensed consolidated financial statements.

Sally Beauty Holdings, Inc. and Subsidiaries

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Basis of Presentation

The condensed consolidated interim financial statements included herein have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) and pursuant to the rules and regulations of the SEC. Accordingly, certain information and note disclosures normally included in annual financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to the rules and regulations of the SEC, although we believe that the disclosures are adequate to make the information not misleading. These condensed consolidated interim financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended September 30, 2018. In the opinion of management, these condensed consolidated interim financial statements reflect all adjustments that are of a normal recurring nature and which are necessary to present fairly our consolidated financial position as of March 31, 2019 and September 30, 2018, our consolidated results of operations and consolidated comprehensive income for the three and six months ended March 31, 2019 and 2018, and our consolidated cash flows for six months ended March 31, 2019 and 2018.

Certain amounts for the prior year have been conformed to the current year’s presentation.

2. Significant Accounting Policies

We adhere to the same accounting policies in the preparation of our condensed consolidated interim financial statements as we do in the preparation of our full-year consolidated financial statements. As permitted under GAAP, interim accounting for certain expenses, including income taxes, is based on full-year assumptions. For interim financial reporting purposes, income taxes are recorded based upon estimated annual effective income tax rates.

3. Accounting Changes and Recent Accounting Pronouncements

Accounting Changes

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (“ASU No. 2014-09”), which introduced new guidance that established how an entity should measure revenue in connection with its sale of goods and services to a customer based on the consideration to which the entity expects to be entitled in exchange for each of those goods and services. On October 1, 2018, we adopted ASU No. 2014-09 using the modified retrospective transition method. Additionally, in connection with the adoption, we designed changes to our internal control procedures and updated processes to ensure appropriate recognition and presentation of financial information. This adoption did not have a material effect on our consolidated financial statements or on our internal controls over financial reporting. We do not believe that the adoption will have a material effect on our consolidated financial statements on an ongoing basis. The comparative periods continue to be presented under the accounting standards in effect during those periods.

In connection with the adoption of ASU No. 2014-09, we now present our sales returns allowance on a gross basis rather than a net liability basis. As such, we recognize a return asset from the right to recover merchandise from

customers (included in other current assets) and a return liability from the amount to be returned to the customer (included in accrued liabilities) within our consolidated balance sheets. Additionally, we now recognize revenue for our gift cards not expected to be redeemed (“gift card breakage”) within revenue in our consolidated statements of earnings.

The following tables set forth the impact of adopting this standard on our condensed consolidated balance sheets as of March 31, 2019 and our condensed consolidated statements of earnings for the three and six months ended March 31, 2019 (in thousands):

Effect of ASU No. 2014-09 Adoption on Condensed Consolidated Balance Sheet

|                      | As reported | Excluding ASU No. 2014-09 Effect | ASU No. 2014-09 Effect |
|----------------------|-------------|----------------------------------|------------------------|
| Other current assets | \$39,895    | \$37,256                         | \$2,639                |
| Accrued liabilities  | \$156,490   | \$153,851                        | \$2,639                |

## Effect of ASU No. 2014-09 Adoption on Condensed Consolidated Statement of Earnings

For the three months ended March 31, 2019

|                                              | As reported | Excluding ASU No. 2014-09 Effect | ASU No. 2014-09 Effect |
|----------------------------------------------|-------------|----------------------------------|------------------------|
| Net Sales                                    | \$945,852   | \$945,752                        | \$ 100                 |
| Gross Profit                                 | 468,324     | 468,224                          | 100                    |
| Selling, general and administrative expenses | \$361,626   | \$361,526                        | \$ 100                 |

For the six months ended March 31, 2019

|                                              | As reported | Excluding ASU No. 2014-09 Effect | ASU No. 2014-09 Effect |
|----------------------------------------------|-------------|----------------------------------|------------------------|
| Net Sales                                    | \$1,935,305 | \$1,935,130                      | \$ 175                 |
| Gross Profit                                 | 949,030     | 948,855                          | 175                    |
| Selling, general and administrative expenses | \$728,614   | \$728,439                        | \$ 175                 |

See note 4, Revenue Recognition, for additional information related to ASU No. 2014-09.

## Recent Accounting Pronouncements

In February 2016, the FASB issued ASU No. 2016-02, Leases, which will require most leases to be reported on the balance sheet as a right-of-use asset and a lease liability. Under the new guidance, the lease liability must be measured initially based on the present value of future lease payments, subject to certain conditions. The right-of-use asset must be measured initially based on the amount of the liability, plus certain initial direct costs. The new guidance further requires that leases be classified at inception as either (a) operating leases or (b) finance leases. For operating leases, periodic expense will generally be flat (straight-line) throughout the life of the lease. For finance leases, periodic expense will decline (similar to capital leases under prior rules) over the life of the lease. The new standard must be adopted using a modified retrospective transition method, but companies can adopt using the effective date method or the comparative method. For public companies, this standard is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. We will adopt this pronouncement on October 1, 2019 using the effective date method. We have completed a preliminary assessment of the potential impact of adopting ASU No. 2016-02 on our consolidated financial statements. At March 31, 2019, adoption of ASU No. 2016-02 would have resulted in recognition of a right-of-use asset in the estimated amount of approximately \$525.0 million and a lease liability for a similar amount in our consolidated balance sheet. We are currently in the process of implementing changes to our processes, controls and systems in order to be compliant upon adoption of the new standard. We do not believe adoption of ASU No. 2016-02 will have a material impact on our consolidated results of operations or consolidated cash flows. The amount of the right-of-use asset and the lease liability we ultimately recognize may materially differ from this preliminary estimate, including as a result of future organic growth in our business, changes



in interest rates, and potential acquisitions.

#### 4. Revenue Recognition

Substantially all of our revenue is derived through the sale of merchandise. Revenue is recognized net of estimated sales returns and sales taxes. We estimate sales returns based on historical data. Additionally, we have assessed all revenue streams for principal versus agent considerations and have concluded we are the principal for all transactions.

See Note 13, Business Segments, for additional information regarding the disaggregation of our sales revenue.

##### Merchandise Revenues

The majority of our revenue comes from the sale of products in our company-operated stores. These sales generally have one single performance obligation and the revenue is recognized at the point of sale. Discounts and incentives issued at the point of sale to entice a customer to a future purchase are treated as a separate performance obligation. As such, we allocate a portion of the revenue generated from the point of sale to each of the additional performance obligations separately using explicitly stated amounts or our best estimate using historical data.

We also sell merchandise on our online platforms, to our franchisees and by using distributor sales consultants. These sales generally have one single performance obligation and revenue is recognized upon the shipment of the merchandise. Any shipping and handling fees charged to the customer are recognized as revenue, while any shipping and handling costs to get the merchandise shipped is recognized in cost of goods sold.

We do extend credit to certain customers, primarily salon professionals, which generally have 30 day payment terms. Based on the nature of these receivables, no significant financing component exists.

#### Gift Cards

The revenue from the sale of our gift cards is recognized at the time the gift card is used to purchase merchandise, which is generally within one year from the date of purchase. Our gift cards do not carry expiration dates or impose post-sale fees. Based on historical experience, a certain amount of our gift cards will not be redeemed, also referred to as “gift card breakage.” We recognize revenue related to gift card breakage within revenue in our consolidated statements of earnings over time proportionately to historical redemption patterns. The gift cards are issued and represent liabilities of either of our operating entities, Sally Beauty Supply LLC or Beauty Systems Group LLC, which are both limited liability companies formed in the state of Virginia.

#### Customer Loyalty Rewards

We recently launched our new Sally Beauty Rewards Loyalty Program nationwide during the first quarter of fiscal year 2019 to the U.S. and Canada, which enables customers to earn points based on their status for every dollar spent on merchandise purchased in our Sally Beauty Supply (“SBS”) stores and through our sallybeauty.com website. When a specific tier has been reached, a customer will receive a certificate which can be used at any of our U.S. and Canada SBS stores or through our sallybeauty.com website on their next purchase. Based on the rewards loyalty program policies, points expire after twelve months of inactivity and certificates will expire after a specific time period from the date of issuance. Certificates generated from our rewards loyalty program provide a material right to customers and represent a separate performance obligation. Rewards loyalty points are accrued at the standalone value per point, net of estimated breakage, and are included within accrued liabilities on our consolidated balance sheets. We recognize the revenue when the customer redeems the certificate. Points and certificates are issued by and represent liabilities of Sally Beauty Supply LLC.

The following table shows the amount of our gift card and rewards loyalty program liabilities included in accrued liabilities within our condensed consolidated balance sheets as of March 31, 2019 and September 30, 2018 (in thousands):

|                         | March<br>31,    | September<br>30, |
|-------------------------|-----------------|------------------|
|                         | 2019            | 2018             |
| Gift cards              | \$4,528         | \$ 4,144         |
| Rewards loyalty program | 7,032           | 1,165            |
| <b>Total liability</b>  | <b>\$11,560</b> | <b>\$ 5,309</b>  |

#### 5. Fair Value Measurements

##### Fair value on recurring basis

Consistent with the three-level hierarchy defined in ASC Topic 820, Fair Value Measurement, as amended, we categorize our financial assets and liabilities as follows (in thousands):

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|                            |         | As of<br>March<br>31,<br>2019 | As of<br>September<br>30, 2018 |
|----------------------------|---------|-------------------------------|--------------------------------|
| <b>Assets</b>              |         |                               |                                |
| Foreign exchange contracts | Level 2 | \$580                         | \$ —                           |
| Interest rate caps         | Level 2 | 1,636                         | 8,367                          |
| Total assets               |         | \$2,216                       | \$ 8,367                       |
| <b>Liabilities</b>         |         |                               |                                |
| Foreign exchange contracts | Level 2 | \$333                         | \$ —                           |

Other fair value disclosures

|                       |         | As of March 31, 2019 |             | As of September 30,<br>2018 |             |
|-----------------------|---------|----------------------|-------------|-----------------------------|-------------|
|                       |         | Carrying<br>Value    | Fair Value  | Carrying<br>Value           | Fair Value  |
| <b>Long-term debt</b> |         |                      |             |                             |             |
| Senior notes          | Level 1 | \$889,946            | \$888,694   | \$950,000                   | \$911,490   |
| Other long-term debt  | Level 2 | 842,606              | 823,421     | 845,383                     | 824,951     |
| Total debt            |         | \$1,732,552          | \$1,712,115 | \$1,795,383                 | \$1,736,441 |

## 6. Accumulated Other Comprehensive Loss

The change in accumulated other comprehensive loss (“AOCL”) was as follows (in thousands):

|                                                              | Foreign<br>Currency<br>Translation<br>Adjustments | Interest<br>Rate<br>Caps | Foreign<br>Exchange<br>Contracts | Total       |
|--------------------------------------------------------------|---------------------------------------------------|--------------------------|----------------------------------|-------------|
| Balance at September 30, 2018                                | \$ (91,356 )                                      | \$ 1,365                 | \$ —                             | \$(89,991 ) |
| Other comprehensive loss before reclassification, net of tax | (10,425 )                                         | (5,014)                  | (253 )                           | (15,692 )   |
| Reclassification to net earnings, net of tax                 | —                                                 | 44                       | 85                               | 129         |
| Balance at March 31, 2019                                    | \$ (101,781 )                                     | \$(3,605)                | \$ (168 )                        | \$(105,554) |

The tax impact for the changes in other comprehensive loss and the reclassifications to net earnings were not material.

## 7. Weighted Average Shares

The following table sets forth the computations of basic and diluted earnings per share (in thousands):

|                                       | Three Months<br>Ended |         | Six Months Ended  |         |
|---------------------------------------|-----------------------|---------|-------------------|---------|
|                                       | March 31,<br>2019     | 2018    | March 31,<br>2019 | 2018    |
| Weighted average basic shares         | 120,077               | 124,270 | 120,033           | 126,046 |
| Dilutive securities:                  |                       |         |                   |         |
| Stock option and stock award programs | 914                   | 787     | 916               | 788     |
| Weighted average diluted shares       | 120,991               | 125,057 | 120,949           | 126,834 |

For the three and six months ended March 31, 2019, options to purchase 5.2 million shares of our common stock were outstanding but not included in our computations of diluted earnings per share, since these options were anti-dilutive. For the three and six months ended March 31, 2018, options to purchase 5.4 million shares of our common stock were outstanding but not included in the computations of diluted earnings per share, since these options were anti-dilutive.

## 8. Share-Based Payments

## Performance-Based Awards

The following table presents a summary of the activity for our performance unit awards assuming 100% payout:

|                                | Number<br>of Shares | Weighted<br>Average Fair<br>Value Per<br>Share | Weighted<br>Average<br>Remaining<br>Vesting<br>Term<br>(in Years) |
|--------------------------------|---------------------|------------------------------------------------|-------------------------------------------------------------------|
| Performance Unit Awards        | (in Thousands)      |                                                |                                                                   |
| Unvested at September 30, 2018 | 349                 | \$ 20.88                                       | 1.3                                                               |
| Granted                        | 230                 | 17.22                                          |                                                                   |
| Vested                         | (23 )               | 23.45                                          |                                                                   |
| Forfeited                      | (99 )               | 21.68                                          |                                                                   |
| Unvested at March 31, 2019     | 457                 | \$ 18.74                                       | 1.8                                                               |

Service-Based Awards

The following table presents a summary of the activity for our stock option awards:

|                                   | Number of      | Weighted | Weighted   | Aggregate      |
|-----------------------------------|----------------|----------|------------|----------------|
|                                   | Outstanding    | Average  | Remaining  | Intrinsic      |
|                                   | Options        | Exercise | Term       | Value          |
|                                   | (in Thousands) | Price    | (in Years) | (in Thousands) |
| Outstanding at September 30, 2018 | 5,405          | \$ 23.04 | 5.4        | \$ 3,161       |
| Granted                           | 948            | 18.14    |            |                |
| Exercised                         | (127 )         | 15.42    |            |                |
| Forfeited or expired              | (849 )         | 25.32    |            |                |
| Outstanding at March 31, 2019     | 5,377          | \$ 21.99 | 6.3        | \$ 2,924       |
| Exercisable at March 31, 2019     | 3,444          | \$ 23.68 | 4.9        | \$ 1,773       |

The following table presents a summary of the activity for our Restricted Stock Awards:

|                                | Number         | Weighted  | Weighted   |
|--------------------------------|----------------|-----------|------------|
|                                | of Shares      | Average   | Remaining  |
|                                |                | Fair      | Vesting    |
|                                |                | Value Per | Term       |
| Restricted Stock Awards        | (in Thousands) | Share     | (in Years) |
| Unvested at September 30, 2018 | 219            | \$ 16.98  | 2.1        |
| Granted                        | 287            | 18.14     |            |
| Vested                         | (6 )           | 18.29     |            |
| Forfeited                      | (31 )          | 17.64     |            |
| Unvested at March 31, 2019     | 469            | \$ 17.60  | 2.1        |

The following table presents a summary of the activity for our Restricted Stock Units:

|                                |                | Weighted  |            |
|--------------------------------|----------------|-----------|------------|
|                                | Number         | Average   | Remaining  |
|                                | of Shares      | Fair      | Vesting    |
|                                |                | Value Per | Term       |
| Restricted Stock Units         | (in Thousands) | Share     | (in Years) |
| Unvested at September 30, 2018 | —              | \$ —      | —          |
| Granted                        | 88             | 18.14     |            |
| Vested                         | —              | —         |            |
| Forfeited                      | —              | —         |            |
| Unvested at March 31, 2019     | 88             | \$ 18.14  | 0.5        |

## 9. Goodwill and Intangible Assets

During the three months ended March 31, 2019 we completed our annual assessment for impairment of goodwill and other intangible assets. No material impairment losses were recognized in the current or prior periods presented in connection with our goodwill and other intangible assets.

For the three months ended March 31, 2019 and 2018, amortization expense related to other intangible assets was \$2.9 million and \$2.7 million, respectively, and, for the six months ended March 31, 2019 and 2018, amortization expense was \$5.7 million and \$5.6 million, respectively.

During the six months ended March 31, 2019, we recorded approximately \$1.9 million in other intangible assets related to immaterial asset acquisitions. Additionally, goodwill and other intangible assets were negatively impacted from changes in foreign currency exchange rates of approximately \$2.6 million and \$0.6 million, respectively.

## 10. Short-term Borrowings and Long-term Debt

At March 31, 2019, we had \$481.9 million available for borrowing under our five-year asset-based senior secured loan facility (the “ABL facility”), including the Canadian sub-facility. At March 31, 2019, we were in compliance with the agreements and instruments governing our debt, including our financial covenants.

During the three months ended March 31, 2019, we commenced tender offer for up to \$100.0 million in aggregate purchase price of our 5.625% Senior Notes due 2025 (the “2025 Notes”) with a sublimit of \$25.0 million for purchase of our 5.500% Senior Notes due 2023 (the “2023 Notes”), in each case issued by our indirect wholly-owned subsidiaries Sally Holdings LLC and Sally Capital Inc. (“Tender Offer”). As a result of the Tender Offer, we repurchased approximately \$57.5 million aggregate principal amount of the 2025 Notes and approximately \$2.6 million aggregate principal amount of the 2023 Notes at a total tender offer price of 98.0% and 100.0%, respectively, excluding accrued interest. In connection with the Tender Offer, we recognized a \$0.5 million gain on the extinguishment of debt, including a gain of approximately \$1.2 million from the discount paid under the face value of the accepted 2025 Notes and the write off of \$0.7 million in unamortized deferred financing costs.

## 11. Derivative Instruments and Hedging Activities

During the six months ended March 31, 2019, we did not purchase or hold any derivative instruments for trading or speculative purposes.

### Designated Cash Flow Hedges

### Foreign Currency Forwards

In December 2018, we entered into foreign currency forwards to mitigate the exposure to exchange rate changes on inventory purchases in USD by our foreign subsidiaries. At March 31, 2019, the notional amount we held through these forwards, based upon exchange rates at March 31, 2019, was as follows (in thousands):

| Notional Currency | Notional Amount |
|-------------------|-----------------|
| MXP               | \$ 15,310       |
| EUR               | 10,916          |
| CAD               | 7,507           |
| GBP               | 4,511           |
| Total             | \$ 38,244       |

We record quarterly, net of income tax, the changes in fair value related to the foreign currency forwards into AOCL. As the forwards are exercised, the realized value will be recognized into cost of goods sold based on inventory turns. Based on March 31, 2019 valuations and exchange rates, we expect to reclassify approximately \$0.5 million into cost of goods sold over the next 12 months.

### Interest Rate Caps



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In July 2017, we purchased two interest rate caps with an initial aggregate notional amount of \$550 million (the “interest rate caps”) to mitigate the exposure to increasing interest rates in connection with our term loan B. The interest rate caps are comprised of individual caplets that expire ratably through June 30, 2023 and are designated as cash flow hedges. Accordingly, changes in fair value of the interest rate caps are recorded quarterly, net of income tax, and are included in AOCL. Over the next 12 months, we expect to reclassify approximately \$0.5 million into interest expense, which represents the original value of the expiring caplets.

The table below presents the fair value of our derivative financial instruments (in thousands):

|                                                | Asset Derivatives    |                    | Liability Derivatives |                     |        |      |
|------------------------------------------------|----------------------|--------------------|-----------------------|---------------------|--------|------|
|                                                | March 31, 2019       | September 30, 2018 | March 31, 2019        | September 30, 2018  |        |      |
| Derivatives designated as hedging instruments: |                      |                    |                       |                     |        |      |
| Interest rate caps                             | Other assets         | \$ 1,636           | \$ 8,367              | N/A                 | \$ —   | \$ — |
| Foreign exchange contracts                     | Other current assets | 580                | —                     | Accrued liabilities | 333    | —    |
|                                                |                      | \$2,216            | \$ 8,367              |                     | \$ 333 | \$ — |

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The effects of our derivative financial instruments on our condensed consolidated statements of earnings were not material for the three and six months ended March 31, 2019 and 2018.

## 12. Income Taxes

Our effective tax rate for the three months ended March 31, 2019 and 2018 was 25.9% and 28.5%, respectively. For the three months ended March 31, 2019, our effective tax rate was favorably impacted by a lower federal statutory rate when compared the prior year as a result of the Tax Cut and Jobs Act (“U.S. Tax Reform”). For the fiscal year 2019, our U.S. federal statutory rate will be 21.0% compared to 24.5% for the prior fiscal year.

Our effective tax rate for the six months ended March 31, 2019 and 2018 was 24.4% and 15.9%, respectively. For the six months ended March 31, 2018, our effective tax rate was favorably impacted by a net income tax benefit of \$22.2 million related to U.S. Tax Reform when compared to the current period. This benefit was partially offset by the lower federal statutory rates recorded in the current period as compared to the prior period.

In December 2017, the SEC issued Staff Accounting Bulletin No. 118 (“SAB 118”) which provided guidance allowing registrants to record provisional amounts, during a specified measurement period, when the necessary information is not available, prepared or analyzed in reasonable detail to account for the impact of U.S. Tax Reform. As of December 31, 2018, we have completed our analysis on our provisional calculations within the measurement period provided by SAB 118. As a result, during the six months ended March 31, 2019, we identified certain immaterial adjustments to our provisional calculations, including a benefit of \$3.0 million related to the transition tax on unremitted earnings of our foreign operations.

In addition, the U.S. Treasury Department has recently released proposed regulations covering the one-time transition tax on unrepatriated foreign earnings, which was enacted as part of the U.S. Tax Reform. Included within the proposed regulations, certain guidance is inconsistent with our interpretation of the enacted tax law. This proposed regulation is not authoritative and is subject to change in the regulatory review process. However, if the proposed regulation is included in the final regulations as drafted, we may be required to reverse \$2.5 million of benefit in the quarter the regulations become final.

Beginning in our first quarter of fiscal year 2019, we are subject to taxation on global intangible low-taxed income (“GILTI”) earned by certain foreign subsidiaries. We have made the policy election to record this tax as a period cost at the time it is incurred. The impact from GILTI was immaterial for the three months ended March 31, 2019 and is expected to be immaterial for the full fiscal year 2019.

## 13. Business Segments

Segment data for the three and six months ended March 31, 2019 and 2018 is as follows (in thousands):

| Three Months Ended |      | Six Months Ended  |      |
|--------------------|------|-------------------|------|
| March 31,<br>2019  | 2018 | March 31,<br>2019 | 2018 |

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|                                             |           |           |             |             |
|---------------------------------------------|-----------|-----------|-------------|-------------|
| Net sales:                                  |           |           |             |             |
| SBS                                         | \$565,604 | \$580,114 | \$1,146,213 | \$1,165,689 |
| Beauty Systems Group ("BSG")                | 380,248   | 395,207   | 789,092     | 804,597     |
| Total                                       | \$945,852 | \$975,321 | \$1,935,305 | \$1,970,286 |
| Earnings before provision for income taxes: |           |           |             |             |
| Segment operating earnings:                 |           |           |             |             |
| SBS                                         | \$86,715  | \$90,328  | \$176,706   | \$176,922   |
| BSG                                         | 56,518    | 59,949    | 118,849     | 124,514     |
| Segment operating earnings                  | 143,233   | 150,277   | 295,555     | 301,436     |
| Unallocated expenses                        | (36,535 ) | (32,416 ) | (75,139 )   | (68,233 )   |
| Restructuring                               | 5,814     | (6,759 )  | 1,834       | (11,969 )   |
| Consolidated operating earnings             | 112,512   | 111,102   | 222,250     | 221,234     |
| Interest expense                            | (23,821 ) | (25,262 ) | (48,310 )   | (49,277 )   |
| Earnings before provision for income taxes  | \$88,691  | \$85,840  | \$173,940   | \$171,957   |

Sales between segments, which are eliminated in consolidation, were not material during the three and six months ended March 31, 2019 and 2018.

## Disaggregation of net sales by segment

|                                | Three Months<br>Ended |        | Six Months<br>Ended |        |
|--------------------------------|-----------------------|--------|---------------------|--------|
| SBS                            | March 31,             |        | March 31,           |        |
|                                | 2019                  | 2018   | 2019                | 2018   |
| Hair color                     | 29.1 %                | 26.9 % | 28.3 %              | 26.6 % |
| Hair care                      | 20.5 %                | 21.3 % | 20.2 %              | 20.9 % |
| Skin and nail care             | 14.6 %                | 14.8 % | 14.8 %              | 14.9 % |
| Styling tools                  | 13.6 %                | 14.0 % | 14.7 %              | 14.7 % |
| Salon supplies and accessories | 7.5 %                 | 7.5 %  | 7.3 %               | 7.3 %  |
| Multicultural products         | 7.0 %                 | 7.2 %  | 6.7 %               | 6.9 %  |
| Other Beauty items             | 7.7 %                 | 8.3 %  | 8.0 %               | 8.6 %  |
| Total                          | 100.0%                | 100.0% | 100.0%              | 100.0% |

|                    | Three Months<br>Ended |        | Six Months<br>Ended |        |
|--------------------|-----------------------|--------|---------------------|--------|
| BSG                | March 31,             |        | March 31,           |        |
|                    | 2019                  | 2018   | 2019                | 2018   |
| Hair color         | 40.3 %                | 38.7 % | 39.1 %              | 37.8 % |
| Hair care          | 34.2 %                | 34.0 % | 33.8 %              | 33.8 % |
| Skin and nail care | 8.2 %                 | 8.8 %  | 8.2 %               | 8.9 %  |
| Styling tools      | 3.2 %                 | 3.7 %  | 3.6 %               | 4.2 %  |
| Other beauty items | 6.6 %                 | 6.6 %  | 6.1 %               | 6.1 %  |
| Promotional items  | 7.5 %                 | 8.2 %  | 9.2 %               | 9.2 %  |
| Total              | 100.0%                | 100.0% | 100.0%              | 100.0% |

## 14. Parent, Issuers, Guarantor and Non-Guarantor Condensed Consolidating Financial Statements

## Condensed Consolidating Balance Sheet

March 31, 2019

(In thousands)

|                                                                 | Sally<br>Holdings LLC<br>and Sally |                     | Non-<br>Guarantor<br>Guarantor | Consolidating     | Sally Beauty<br>Holdings,<br>Inc. and<br>Subsidiaries |                     |
|-----------------------------------------------------------------|------------------------------------|---------------------|--------------------------------|-------------------|-------------------------------------------------------|---------------------|
|                                                                 | Parent                             | Capital Inc.        | Subsidiaries                   | Eliminations      | Subsidiaries                                          |                     |
| <b>Assets</b>                                                   |                                    |                     |                                |                   |                                                       |                     |
| Cash and cash equivalents                                       | \$—                                | \$ 10               | \$49,719                       | \$ 40,048         | \$—                                                   | \$ 89,777           |
| Trade and other accounts<br>receivable, net                     | —                                  | —                   | 57,983                         | 33,444            | —                                                     | 91,427              |
| Due from affiliates                                             | —                                  | —                   | 2,691,139                      | —                 | (2,691,139 )                                          | —                   |
| Inventory                                                       | —                                  | —                   | 714,757                        | 238,286           | —                                                     | 953,043             |
| Other current assets                                            | 2,906                              | 196                 | 23,399                         | 13,394            | —                                                     | 39,895              |
| Property and equipment, net                                     | 6                                  | —                   | 230,007                        | 67,111            | —                                                     | 297,124             |
| Investment in subsidiaries                                      | 1,489,197                          | 4,206,154           | 381,353                        | —                 | (6,076,704 )                                          | —                   |
| Goodwill and other intangible<br>assets, net                    | —                                  | —                   | 456,574                        | 145,362           | —                                                     | 601,936             |
| Other assets                                                    | 1,325                              | 3,303               | (3,441 )                       | 18,225            | —                                                     | 19,412              |
| <b>Total assets</b>                                             | <b>\$ 1,493,434</b>                | <b>\$ 4,209,663</b> | <b>\$ 4,601,490</b>            | <b>\$ 555,870</b> | <b>\$(8,767,843 )</b>                                 | <b>\$ 2,092,614</b> |
| <b>Liabilities and Stockholders'<br/>(Deficit) Equity</b>       |                                    |                     |                                |                   |                                                       |                     |
| Accounts payable                                                | \$85                               | \$ 3,456            | \$ 197,401                     | \$ 51,528         | \$—                                                   | \$ 252,470          |
| Due to affiliates                                               | 1,626,428                          | 982,434             | —                              | 82,277            | (2,691,139 )                                          | —                   |
| Accrued liabilities                                             | 359                                | 21,520              | 103,095                        | 31,516            | —                                                     | 156,490             |
| Income taxes payable                                            | 5,093                              | 1,519               | —                              | (332 )            | —                                                     | 6,280               |
| Long-term debt                                                  | —                                  | 1,713,068           | 3                              | 853               | —                                                     | 1,713,924           |
| Other liabilities                                               | 6,729                              | —                   | 15,303                         | 3,885             | —                                                     | 25,917              |
| Deferred income tax<br>liabilities, net                         | (185 )                             | (1,531 )            | 79,534                         | 4,790             | —                                                     | 82,608              |
| <b>Total liabilities</b>                                        | <b>1,638,509</b>                   | <b>2,720,466</b>    | <b>395,336</b>                 | <b>174,517</b>    | <b>(2,691,139 )</b>                                   | <b>2,237,689</b>    |
| <b>Total stockholders' (deficit)<br/>equity</b>                 | <b>(145,075 )</b>                  | <b>1,489,197</b>    | <b>4,206,154</b>               | <b>381,353</b>    | <b>(6,076,704 )</b>                                   | <b>(145,075 )</b>   |
| <b>Total liabilities and<br/>stockholders' (deficit) equity</b> | <b>\$ 1,493,434</b>                | <b>\$ 4,209,663</b> | <b>\$ 4,601,490</b>            | <b>\$ 555,870</b> | <b>\$(8,767,843 )</b>                                 | <b>\$ 2,092,614</b> |



## Condensed Consolidating Balance Sheet

September 30, 2018

(In thousands)

|                                                                 | Parent              | Sally<br>Holdings LLC<br>and Sally<br>Capital Inc. | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Consolidating<br>Eliminations | Sally<br>Beauty<br>Holdings,<br>Inc. and<br>Subsidiaries |
|-----------------------------------------------------------------|---------------------|----------------------------------------------------|---------------------------|-----------------------------------|-------------------------------|----------------------------------------------------------|
| <b>Assets</b>                                                   |                     |                                                    |                           |                                   |                               |                                                          |
| Cash and cash equivalents                                       | \$—                 | \$ 10                                              | \$ 29,050                 | \$ 48,235                         | \$—                           | \$ 77,295                                                |
| Trade and other accounts<br>receivable, net                     | 4                   | —                                                  | 53,295                    | 37,191                            | —                             | 90,490                                                   |
| Due from affiliates                                             | —                   | —                                                  | 2,598,681                 | —                                 | (2,598,681 )                  | —                                                        |
| Inventory                                                       | —                   | —                                                  | 714,000                   | 230,338                           | —                             | 944,338                                                  |
| Other current assets                                            | 2,010               | 111                                                | 27,422                    | 13,417                            | —                             | 42,960                                                   |
| Property and equipment, net                                     | 8                   | —                                                  | 232,941                   | 75,408                            | —                             | 308,357                                                  |
| Investment in subsidiaries                                      | 1,368,927           | 4,044,669                                          | 380,166                   | —                                 | (5,793,762 )                  | —                                                        |
| Goodwill and other intangible<br>assets, net                    | —                   | —                                                  | 459,348                   | 149,275                           | —                             | 608,623                                                  |
| Other assets                                                    | 1,325               | 10,242                                             | (4,797 )                  | 18,581                            | —                             | 25,351                                                   |
| <b>Total assets</b>                                             | <b>\$ 1,372,274</b> | <b>\$ 4,055,032</b>                                | <b>\$ 4,490,106</b>       | <b>\$ 572,445</b>                 | <b>\$ (8,392,443 )</b>        | <b>\$ 2,097,414</b>                                      |
| <b>Liabilities and Stockholders'</b>                            |                     |                                                    |                           |                                   |                               |                                                          |
| <b>(Deficit) Equity</b>                                         |                     |                                                    |                           |                                   |                               |                                                          |
| Accounts payable                                                | \$ 38               | \$ -                                               | \$ 233,936                | \$ 69,267                         | \$—                           | \$ 303,241                                               |
| Due to affiliates                                               | 1,629,411           | 888,141                                            | —                         | 81,129                            | (2,598,681 )                  | —                                                        |
| Accrued liabilities                                             | 234                 | 23,019                                             | 125,179                   | 31,855                            | —                             | 180,287                                                  |
| Income taxes payable                                            | 585                 | 1,519                                              | —                         | 40                                | —                             | 2,144                                                    |
| Long-term debt                                                  | —                   | 1,773,426                                          | 1                         | 882                               | —                             | 1,774,309                                                |
| Other liabilities                                               | 10,562              | —                                                  | 15,250                    | 4,210                             | —                             | 30,022                                                   |
| Deferred income tax liabilities,<br>net                         | —                   | —                                                  | 71,071                    | 4,896                             | —                             | 75,967                                                   |
| <b>Total liabilities</b>                                        | <b>1,640,830</b>    | <b>2,686,105</b>                                   | <b>445,437</b>            | <b>192,279</b>                    | <b>(2,598,681 )</b>           | <b>2,365,970</b>                                         |
| <b>Total stockholders' (deficit)<br/>equity</b>                 | <b>(268,556 )</b>   | <b>1,368,927</b>                                   | <b>4,044,669</b>          | <b>380,166</b>                    | <b>(5,793,762 )</b>           | <b>(268,556 )</b>                                        |
| <b>Total liabilities and<br/>stockholders' (deficit) equity</b> | <b>\$ 1,372,274</b> | <b>\$ 4,055,032</b>                                | <b>\$ 4,490,106</b>       | <b>\$ 572,445</b>                 | <b>\$ (8,392,443 )</b>        | <b>\$ 2,097,414</b>                                      |





## Condensed Consolidating Statement of Earnings and Comprehensive Income

Three Months Ended March 31, 2019

(In thousands)

|                                                   | Sally        |              |              |               | Sally Beauty   |              |
|---------------------------------------------------|--------------|--------------|--------------|---------------|----------------|--------------|
|                                                   | Holdings LLC |              | Non-         |               | Holdings, Inc. |              |
|                                                   | and Sally    | Guarantor    | Guarantor    | Consolidating | and            | Subsidiaries |
|                                                   | Parent       | Capital Inc. | Subsidiaries | Subsidiaries  | Eliminations   | Subsidiaries |
| Net sales                                         | \$ —         | \$ —         | \$ 769,284   | \$ 176,568    | \$ —           | \$ 945,852   |
| Related party sales                               | —            | —            | 480          | —             | (480 )         | —            |
| Cost of products sold and distribution expenses   | —            | —            | 383,147      | 94,861        | (480 )         | 477,528      |
| Gross profit                                      | —            | —            | 386,617      | 81,707        | —              | 468,324      |
| Selling, general and administrative expenses      | 3,084        | 198          | 281,404      | 76,940        | —              | 361,626      |
| Restructuring                                     | —            | —            | (5,814 )     | —             | —              | (5,814 )     |
| Operating earnings (loss)                         | (3,084 )     | (198 )       | 111,027      | 4,767         | —              | 112,512      |
| Interest expense (income)                         | —            | 23,871       | (1 )         | (49 )         | —              | 23,821       |
| Earnings (loss) before provision for income taxes | (3,084 )     | (24,069 )    | 111,028      | 4,816         | —              | 88,691       |
| Provision (benefit) for income taxes              | (791 )       | (6,179 )     | 28,795       | 1,141         | —              | 22,966       |
| Equity in earnings of subsidiaries, net of tax    | 68,018       | 85,908       | 3,675        | —             | (157,601 )     | —            |
| Net earnings                                      | 65,725       | 68,018       | 85,908       | 3,675         | (157,601 )     | 65,725       |
| Other comprehensive income (loss), net of tax     | —            | (2,140 )     | —            | 3,282         | —              | 1,142        |
| Total comprehensive income (loss)                 | \$ 65,725    | \$ 65,878    | \$ 85,908    | \$ 6,957      | \$ (157,601 )  | \$ 66,867    |

## Condensed Consolidating Statement of Earnings and Comprehensive Income

Three Months Ended March 31, 2018

(In thousands)

|                                                   | Sally<br>Holdings LLC<br>and Sally<br>Parent |           | Sally<br>Non-<br>Guarantor<br>Subsidiaries |              | Sally Beauty<br>Holdings,<br>Inc.<br>Consolidating<br>and<br>Subsidiaries |            |
|---------------------------------------------------|----------------------------------------------|-----------|--------------------------------------------|--------------|---------------------------------------------------------------------------|------------|
|                                                   | Capital Inc.                                 | Guarantor | Guarantor                                  | Eliminations |                                                                           |            |
| Net sales                                         | \$ —                                         | \$ —      | \$ 786,743                                 | \$ 188,578   | \$ —                                                                      | \$ 975,321 |
| Related party sales                               | —                                            | —         | 631                                        | —            | (631 )                                                                    | —          |
| Cost of products sold and distribution expenses   | —                                            | —         | 390,891                                    | 98,739       | (631 )                                                                    | 488,999    |
| Gross profit                                      | —                                            | —         | 396,483                                    | 89,839       | —                                                                         | 486,322    |
| Selling, general and administrative expenses      | 2,859                                        | 602       | 279,435                                    | 85,565       | —                                                                         | 368,461    |
| Restructuring                                     | —                                            | —         | 6,759                                      | —            | —                                                                         | 6,759      |
| Operating earnings (loss)                         | (2,859 )                                     | (602 )    | 110,289                                    | 4,274        | —                                                                         | 111,102    |
| Interest expense (income)                         | —                                            | 25,293    | (3 )                                       | (28 )        | —                                                                         | 25,262     |
| Earnings (loss) before provision for income taxes | (2,859 )                                     | (25,895 ) | 110,292                                    | 4,302        | —                                                                         | 85,840     |
| Provision (benefit) for income taxes              | (828 )                                       | (7,499 )  | 30,758                                     | 2,038        | —                                                                         | 24,469     |
| Equity in earnings of subsidiaries, net of tax    | 63,402                                       | 81,798    | 2,264                                      | —            | (147,464 )                                                                | —          |
| Net earnings (loss)                               | 61,371                                       | 63,402    | 81,798                                     | 2,264        | (147,464 )                                                                | 61,371     |
| Other comprehensive income, net of tax            | —                                            | 2,310     | —                                          | 10,437       | —                                                                         | 12,747     |
| Total comprehensive income (loss)                 | \$ 61,371                                    | \$ 65,712 | \$ 81,798                                  | \$ 12,701    | \$ (147,464 )                                                             | \$ 74,118  |

## Condensed Consolidating Statement of Earnings and Comprehensive Income

Six Months Ended March 31, 2019

(In thousands)

|                                                      | Sally<br>Holdings LLC<br>and Sally<br>Parent |           | Sally<br>Capital Inc. | Non-<br>Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Consolidating<br>Eliminations | Sally Beauty<br>Holdings,<br>Inc.<br>and<br>Subsidiaries |
|------------------------------------------------------|----------------------------------------------|-----------|-----------------------|-----------------------------------|-----------------------------------|-------------------------------|----------------------------------------------------------|
| Net sales                                            | \$—                                          | \$—       | \$1,562,814           | \$372,491                         | \$—                               | \$—                           | \$1,935,305                                              |
| Related party sales                                  | —                                            | —         | 1,149                 | —                                 | (1,149)                           | —                             | —                                                        |
| Cost of products sold and<br>distribution expenses   | —                                            | —         | 787,187               | 200,237                           | (1,149)                           | —                             | 986,275                                                  |
| Gross profit                                         | —                                            | —         | 776,776               | 172,254                           | —                                 | —                             | 949,030                                                  |
| Selling, general and<br>administrative expenses      | 5,893                                        | 366       | 567,620               | 154,735                           | —                                 | —                             | 728,614                                                  |
| Restructuring                                        | —                                            | —         | (1,834)               | —                                 | —                                 | —                             | (1,834)                                                  |
| Operating earnings (loss)                            | (5,893)                                      | (366)     | 210,990               | 17,519                            | —                                 | —                             | 222,250                                                  |
| Interest expense (income)                            | —                                            | 48,423    | (2)                   | (111)                             | —                                 | —                             | 48,310                                                   |
| Earnings (loss) before provision<br>for income taxes | (5,893)                                      | (48,789)  | 210,992               | 17,630                            | —                                 | —                             | 173,940                                                  |
| Provision (benefit) for income<br>taxes              | (1,512)                                      | (12,524)  | 54,478                | 2,046                             | —                                 | —                             | 42,488                                                   |
| Equity in earnings of subsidiaries,<br>net of tax    | 135,833                                      | 172,098   | 15,584                | —                                 | (323,515)                         | —                             | —                                                        |
| Net earnings                                         | 131,452                                      | 135,833   | 172,098               | 15,584                            | (323,515)                         | —                             | 131,452                                                  |
| Other comprehensive loss, net of<br>tax              | —                                            | (4,949)   | —                     | (10,614)                          | —                                 | —                             | (15,563)                                                 |
| Total comprehensive income<br>(loss)                 | \$131,452                                    | \$130,884 | \$172,098             | \$4,970                           | \$(323,515)                       | —                             | \$115,889                                                |

## Condensed Consolidating Statement of Earnings and Comprehensive Income

Six Months Ended March 31, 2018

(In thousands)

|                                                      | Sally<br>Holdings LLC<br>and Sally<br>Parent |           | Non-<br>Guarantor<br>Subsidiaries |           | Consolidating<br>Eliminations | Sally Beauty<br>Holdings,<br>Inc.<br>and<br>Subsidiaries |
|------------------------------------------------------|----------------------------------------------|-----------|-----------------------------------|-----------|-------------------------------|----------------------------------------------------------|
| Net sales                                            | \$—                                          | \$—       | \$1,583,275                       | \$387,011 | \$—                           | \$1,970,286                                              |
| Related party sales                                  | —                                            | —         | 1,077                             | —         | (1,077)                       | —                                                        |
| Cost of products sold and<br>distribution expenses   | —                                            | —         | 794,701                           | 203,711   | (1,077)                       | 997,335                                                  |
| Gross profit                                         | —                                            | —         | 789,651                           | 183,300   | —                             | 972,951                                                  |
| Selling, general and administrative<br>expenses      | 5,465                                        | 781       | 563,902                           | 169,600   | —                             | 739,748                                                  |
| Restructuring                                        | —                                            | —         | 11,969                            | —         | —                             | 11,969                                                   |
| Operating earnings (loss)                            | (5,465)                                      | (781)     | 213,780                           | 13,700    | —                             | 221,234                                                  |
| Interest expense (income)                            | —                                            | 49,307    | (3)                               | (27)      | —                             | 49,277                                                   |
| Earnings (loss) before provision<br>for income taxes | (5,465)                                      | (50,088)  | 213,783                           | 13,727    | —                             | 171,957                                                  |
| Provision (benefit) for income<br>taxes              | (1,079)                                      | (14,424)  | 22,843                            | 19,982    | —                             | 27,322                                                   |
| Equity in earnings of subsidiaries,<br>net of tax    | 149,021                                      | 184,685   | (6,255)                           | —         | (327,451)                     | —                                                        |
| Net earnings (loss)                                  | 144,635                                      | 149,021   | 184,685                           | (6,255)   | (327,451)                     | 144,635                                                  |
| Other comprehensive income, net<br>of tax            | —                                            | 1,507     | —                                 | 10,182    | —                             | 11,689                                                   |
| Total comprehensive income<br>(loss)                 | \$144,635                                    | \$150,528 | \$184,685                         | \$3,927   | \$(327,451)                   | \$156,324                                                |

## Condensed Consolidating Statement of Cash Flows

Six Months Ended March 31, 2019

(In thousands)

|                                                                      | Sally<br>Holdings LLC<br>and Sally<br>Parent |              | Capital Inc. | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Consolidating<br>Eliminations | Sally Beauty<br>Holdings,<br>Inc.<br>and<br>Subsidiaries |
|----------------------------------------------------------------------|----------------------------------------------|--------------|--------------|---------------------------|-----------------------------------|-------------------------------|----------------------------------------------------------|
| Net cash provided (used) by operating activities                     | \$ 1,262                                     | \$ (32,639 ) | \$ 144,685   | \$ (3,198 )               | \$ —                              |                               | \$ 110,110                                               |
| Cash Flows from Investing Activities:                                |                                              |              |              |                           |                                   |                               |                                                          |
| Payments for property and equipment                                  | —                                            | —            | (41,559 )    | (4,839 )                  | —                                 |                               | (46,398 )                                                |
| Proceeds from sale of property and equipment                         | —                                            | —            | 12,007       | 3                         | —                                 |                               | 12,010                                                   |
| Acquisitions, net of cash acquired                                   | —                                            | —            | (2,008 )     | (840 )                    | —                                 |                               | (2,848 )                                                 |
| Due from affiliates                                                  | —                                            | —            | (92,458 )    | —                         | 92,458                            |                               | —                                                        |
| Net cash used by investing activities                                | —                                            | —            | (124,018 )   | (5,676 )                  | 92,458                            |                               | (37,236 )                                                |
| Cash Flows from Financing Activities:                                |                                              |              |              |                           |                                   |                               |                                                          |
| Proceeds from issuance of long-term debt                             | —                                            | 242,500      | 4            | —                         | —                                 |                               | 242,504                                                  |
| Repayments of long-term debt                                         | —                                            | (304,154 )   | (2 )         | (1 )                      | —                                 |                               | (304,157 )                                               |
| Repurchases of common stock                                          | —                                            | —            | —            | —                         | —                                 |                               | —                                                        |
| Proceeds from exercises of stock options                             | 1,721                                        | —            | —            | —                         | —                                 |                               | 1,721                                                    |
| Due to affiliates                                                    | (2,983)                                      | 94,293       | —            | 1,148                     | (92,458 )                         |                               | —                                                        |
| Net cash provided (used) by financing activities                     | (1,262)                                      | 32,639       | 2            | 1,147                     | (92,458 )                         |                               | (59,932 )                                                |
| Effect of foreign exchange rate changes on cash and cash equivalents | —                                            | —            | —            | (460 )                    | —                                 |                               | (460 )                                                   |
| Net increase (decrease) in cash and cash equivalents                 | —                                            | —            | 20,669       | (8,187 )                  | —                                 |                               | 12,482                                                   |
| Cash and cash equivalents, beginning of period                       | —                                            | 10           | 29,050       | 48,235                    | —                                 |                               | 77,295                                                   |
| Cash and cash equivalents, end of period                             | \$ —                                         | \$ 10        | \$ 49,719    | \$ 40,048                 | \$ —                              |                               | \$ 89,777                                                |



## Condensed Consolidating Statement of Cash Flows

Six Months Ended March 31, 2018

(In thousands)

|                                                                      | Parent    | Sally<br>Holdings LLC<br>and Sally<br>Capital Inc. | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Consolidating<br>Eliminations | Sally Beauty<br>Holdings,<br>Inc.<br>and<br>Subsidiaries |
|----------------------------------------------------------------------|-----------|----------------------------------------------------|---------------------------|-----------------------------------|-------------------------------|----------------------------------------------------------|
| Net cash provided (used) by operating activities                     | \$ 16,313 | \$ (33,119 )                                       | \$ 197,800                | \$ (1,544 )                       | \$ —                          | \$ 179,450                                               |
| Cash Flows from Investing Activities:                                |           |                                                    |                           |                                   |                               |                                                          |
| Payments for property and equipment                                  | —         | —                                                  | (32,092 )                 | (6,601 )                          | —                             | (38,693 )                                                |
| Proceeds from sale of property and equipment                         | —         | —                                                  | —                         | 14                                | —                             | 14                                                       |
| Acquisitions, net of cash acquired                                   | —         | —                                                  | —                         | (9,175 )                          | —                             | (9,175 )                                                 |
| Due from affiliates                                                  | —         | —                                                  | (159,590 )                | —                                 | 159,590                       | —                                                        |
| Net cash used by investing activities                                | —         | —                                                  | (191,682 )                | (15,762 )                         | 159,590                       | (47,854 )                                                |
| Cash Flows from Financing Activities:                                |           |                                                    |                           |                                   |                               |                                                          |
| Proceeds from issuance of long-term debt                             | —         | 246,814                                            | 5                         | —                                 | —                             | 246,819                                                  |
| Repayments of long-term debt                                         | —         | (259,750 )                                         | (2 )                      | (390 )                            | —                             | (260,142 )                                               |
| Debt issuance costs                                                  | —         | (1,151 )                                           | —                         | —                                 | —                             | (1,151 )                                                 |
| Repurchases of common stock                                          | (114,699) | —                                                  | —                         | —                                 | —                             | (114,699 )                                               |
| Proceeds from exercises of stock options                             | 1,112     | —                                                  | —                         | —                                 | —                             | 1,112                                                    |
| Due to affiliates                                                    | 97,274    | 47,206                                             | —                         | 15,110                            | (159,590 )                    | —                                                        |
| Net cash provided (used) by financing activities                     | (16,313 ) | 33,119                                             | 3                         | 14,720                            | (159,590 )                    | (128,061 )                                               |
| Effect of foreign exchange rate changes on cash and cash equivalents | —         | —                                                  | —                         | 762                               | —                             | 762                                                      |
| Net increase (decrease) in cash and cash equivalents                 | —         | —                                                  | 6,121                     | (1,824 )                          | —                             | 4,297                                                    |
| Cash and cash equivalents, beginning of period                       | —         | 10                                                 | 22,090                    | 41,659                            | —                             | 63,759                                                   |

|                                          |     |       |           |           |      |           |
|------------------------------------------|-----|-------|-----------|-----------|------|-----------|
| Cash and cash equivalents, end of period | \$— | \$ 10 | \$ 28,211 | \$ 39,835 | \$ — | \$ 68,056 |
|------------------------------------------|-----|-------|-----------|-----------|------|-----------|



## 15. Restructuring

Restructuring gain and expenses for the three and six months ended March 31, 2019 and 2018, are as follows (in thousands):

|                            | Three Months |         | Six Months Ended |           |
|----------------------------|--------------|---------|------------------|-----------|
|                            | Ended        |         | March 31,        | March 31, |
|                            | 2019         | 2018    | 2019             | 2018      |
| Supply Chain Modernization | \$(5,814)    | \$—     | \$(5,814)        | \$—       |
| 2018 Restructuring Plan    | —            | 6,759   | 3,980            | 11,969    |
| Total expenses (gain)      | \$(5,814)    | \$6,759 | \$(1,834)        | \$11,969  |

## Supply Chain Modernization

In February 2019, we announced that we were assessing our supply chain in an effort to minimize out-of-stocks, optimize inventory levels, reduce cost and explore new replenishment and fulfillment options. As part of our supply chain modernization plans, we sold our secondary headquarters and fulfillment center in Denton, Texas, and anticipate closing select distribution centers and upgrading our e-commerce capabilities. Additionally, we will be opening up a new automated and concentrated distribution center which will service Sally Beauty Supply stores and e-commerce sales as well as Beauty Systems Group stores, full service sales and e-commerce sales.

The liability related to the Supply Chain Modernization, which is included in accrued liabilities in our condensed consolidated balance sheets, is as follows (in thousands):

|                            | Liability at  |          | Cash     |             | Liability at |  |
|----------------------------|---------------|----------|----------|-------------|--------------|--|
|                            | September 30, |          | Payments | Adjustments | March 31,    |  |
| Supply Chain Modernization | 2018          | Expenses |          |             | 2019         |  |
| Workforce reductions       | \$ —          | \$ 236   | \$ 83    | \$ —        | \$ 153       |  |
| Facility closures          | —             | 502      | 502      | —           | —            |  |
| Other                      | —             | 95       | 95       | —           | —            |  |
| Total                      | \$ —          | \$ 833   | \$ 680   | \$ —        | \$ 153       |  |

Expenses incurred in the six months ended March 31, 2019, primarily represent costs incurred by SBS of \$0.6 million.

The above table does not include a gain from selling our secondary headquarters and fulfillment center in Denton, TX of \$6.6 million. In connection with the sale, we leased back the facility at current market rates for an insignificant time while we moved personnel to our primary headquarters.

## 2018 Restructuring Plan

In November 2017, our Board of Directors approved a restructuring plan (the “2018 Restructuring Plan”) focused primarily on significantly improving the profitability of our international businesses, with particular focus on our European operations.

In April 2018, we announced an expansion of the 2018 Restructuring Plan that contained cost reduction initiatives designed to help fund important long-term growth initiatives. The expansion to the 2018 Restructuring Plan included headcount reductions primarily at our corporate headquarters in Denton, Texas. As of December 31, 2018, the 2018 Restructuring Plan was substantially complete and we do not anticipate any additional material costs for the 2018 Restructuring Plan.

The liability related to the 2018 Restructuring Plan, which is included in accrued liabilities in our condensed consolidated balance sheets, is as follows (in thousands):

|                         | Liability at  |          |               |             | Liability at |
|-------------------------|---------------|----------|---------------|-------------|--------------|
|                         | September 30, |          |               |             | March 31,    |
| 2018 Restructuring Plan | 2018          | Expenses | Cash Payments | Adjustments | 2019         |
| Workforce reductions    | \$ 3,444      | \$ 643   | \$ 4,087      | \$ —        | \$ —         |
| Consulting              | 3,087         | 2,502    | 5,589         | —           | —            |
| Other                   | 2,266         | 835      | 2,943         | —           | 158          |
| Total                   | \$ 8,797      | \$ 3,980 | \$ 12,619     | \$ —        | \$ 158       |

Expenses incurred in the six months ended March 31, 2019 represent costs incurred by SBS of \$1.1 million and corporate of \$2.8 million.

## 16. Commitments and Contingencies

We are involved, from time to time, in various claims and lawsuits incidental to the conduct of our business in the ordinary course. We carry insurance coverage in such amounts in excess of our self-insured retention as we believe to be reasonable under the circumstances and that may or may not cover any or all of our liabilities in respect of these matters. We do not believe that the ultimate resolution of these matters will have a material adverse impact on our consolidated financial position, cash flows or results of operations.

### Data Security Incidents

As previously disclosed, we experienced data security incidents during the fiscal years 2014 and 2015 (together, the “data security incidents”). The data security incidents involved the unauthorized installation of malicious software (“malware”) on our information technology systems, including our point-of-sale systems that may have placed at risk certain payment card data for some transactions. The costs that we have incurred to date in connection with the data security incidents include assessments by payment card networks, professional advisory fees and legal fees relating to investigating and remediating the data security incidents.

During the fiscal year ended September 30, 2018, we received an assessment from a payment card network in connection with the data security incidents. The assessment is based on the network’s claims against the Company’s acquiring banks for costs that it asserts its issuing banks incurred in connection with the data security incidents, including incremental counterfeit fraud losses and non-ordinary course operating expenses, such as card reissuance costs. As of March 31, 2019, we have paid the assessment from the payment card network.

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

This section discusses management's view of the financial condition, results of operations and cash flows of Sally Beauty. This section should be read in conjunction with the information contained in our Annual Report on Form 10-K for the fiscal year ended September 30, 2018, including the Risk Factors section, and information contained elsewhere in this Quarterly Report, including the condensed consolidated financial statements and notes to those financial statements. The results of operations for any interim period may not necessarily be indicative of the results that may be expected for any future interim period or the entire fiscal year.

Highlights for the Three Months Ended March 31, 2019:

- Consolidated net sales for the three months ended March 31, 2019, decreased \$29.5 million, or 3.0%, to \$945.9 million, compared to the three months ended March 31, 2018;
- Our global e-commerce sales increased 30.3% compared to the three months ended March 31, 2018;
- Consolidated same store sales decreased 0.5% for the three months ended March 31, 2019. SBS same store sales decreased 0.3% and BSG same store sales decreased 0.9%;
- Consolidated gross profit for the three months ended March 31, 2019 decreased \$18.0 million, or 3.7%, to \$468.3 million compared to the three months ended March 31, 2018. Gross margin decreased 40 basis points to 49.5% for the three months ended March 31, 2019, compared to the three months ended March 31, 2018;
- Consolidated operating earnings for the three months ended March 31, 2019 increased \$1.4 million, or 1.3%, to \$112.5 million compared to the three months ended March 31, 2018. Operating margin increased 50 basis points to 11.9% for the three months ended March 31, 2019, compared to the three months ended March 31, 2018;
- Consolidated net earnings increased \$4.4 million, or 7.1%, to \$65.7 million for the three months ended March 31, 2019 compared to the three months ended March 31, 2018. As a percentage of net sales, net earnings increased 60 basis points to 6.9% for the three months ended March 31, 2019, compared to the three months ended March 31, 2018;
- Diluted earnings per share for the three months ended March 31, 2019, were \$0.54, compared to \$0.49 for the three months ended March 31, 2018;
- Cash provided by operations was \$59.9 million for the three months ended March 31, 2019, compared to \$75.2 million for the three months ended March 31, 2018;
- During the three months ended March 31, 2019, we recognized a net gain within restructuring on our condensed consolidated statements of earnings from our supply chain modernization plan of \$5.8 million, primarily from the sale of our secondary headquarters and fulfillment center in Denton, Texas;
- We repurchased approximately \$60.1 million in senior notes through our debt tender offer and recognized a net gain of approximately \$0.5 million.

Business Strategy Update

We continue to make solid progress on our transformation plan as we initiated our supply chain modernization plans, reduced our debt levels and deployed SBS's new mobile commerce-based App.

During the quarter, we started to roll-out nationwide a new point-of-sale system in both SBS and BSG which will allow our store associates to better serve our customers. Additionally, we are working on deploying a new SBS mobile commerce-based App to enhance our customer's experience and adapt to the way our customers like to shop. As we go forward, we will continue to invest in improving our customer's shopping experience.

In February 2019, we announced our supply chain modernization plans to gain efficiencies and cost savings. During the three months ended March 31, 2019, we sold our secondary headquarters and fulfillment center in Denton, Texas and exited our Anchorage, Alaska distribution center. We continue to explore locations within Texas for the construction of a new 500,000 square foot automated and concentrated distribution center and within Europe for our

distribution operations in Ghent, Belgium.

We recently completed our debt tender offer which reduced our debt levels by \$60.1 million during the three months ended March 31, 2019.

## Overview

## Key Operating Metrics

The following table sets forth, for the periods indicated, information concerning key measures we rely on to evaluate our operating performance (dollars in thousands):

|                                                     | Three Months Ended |           |                        | Six Months Ended |             |                        |            |          |
|-----------------------------------------------------|--------------------|-----------|------------------------|------------------|-------------|------------------------|------------|----------|
|                                                     | March 31,          |           | Increase<br>(Decrease) | March 31,        |             | Increase<br>(Decrease) |            |          |
|                                                     | 2019               | 2018      |                        | 2019             | 2018        |                        |            |          |
| <b>Net sales:</b>                                   |                    |           |                        |                  |             |                        |            |          |
| SBS                                                 | \$565,604          | \$580,114 | \$(14,510)             | (2.5 )%          | \$1,146,213 | \$1,165,689            | \$(19,476) | (1.7 )%  |
| BSG                                                 | 380,248            | 395,207   | (14,959)               | (3.8 )%          | 789,092     | 804,597                | (15,505)   | (1.9 )%  |
| Consolidated                                        | \$945,852          | \$975,321 | \$(29,469)             | (3.0 )%          | \$1,935,305 | \$1,970,286            | \$(34,981) | (1.8 )%  |
| <b>Gross profit:</b>                                |                    |           |                        |                  |             |                        |            |          |
| SBS                                                 | \$314,729          | \$322,565 | \$(7,836 )             | (2.4 )%          | \$631,959   | \$642,351              | \$(10,392) | (1.6 )%  |
| BSG                                                 | 153,595            | 163,757   | (10,162)               | (6.2 )%          | 317,071     | 330,600                | (13,529)   | (4.1 )%  |
| Consolidated                                        | \$468,324          | \$486,322 | \$(17,998)             | (3.7 )%          | \$949,030   | \$972,951              | \$(23,921) | (2.5 )%  |
| <b>Segment gross margin:</b>                        |                    |           |                        |                  |             |                        |            |          |
| SBS                                                 | 55.6 %             | 55.6 %    | —                      | bps              | 55.1 %      | 55.1 %                 | —          | bps      |
| BSG                                                 | 40.4 %             | 41.4 %    | (100)                  | bps              | 40.2 %      | 41.1 %                 | (90)       | bps      |
| Consolidated                                        | 49.5 %             | 49.9 %    | (40)                   | bps              | 49.0 %      | 49.4 %                 | (40)       | bps      |
| <b>Selling, general and administrative expenses</b> |                    |           |                        |                  |             |                        |            |          |
| Restructuring                                       | \$(5,814 )         | \$6,759   | \$(12,573)             | (186.0)%         | \$(1,834 )  | \$11,969               | \$(13,803) | (115.3)% |
| <b>Net earnings:</b>                                |                    |           |                        |                  |             |                        |            |          |
| <b>Segment operating earnings:</b>                  |                    |           |                        |                  |             |                        |            |          |
| SBS                                                 | \$86,715           | \$90,328  | \$(3,613 )             | (4.0 )%          | \$176,706   | \$176,922              | \$(216 )   | (0.1 )%  |
| BSG                                                 | 56,518             | 59,949    | (3,431 )               | (5.7 )%          | 118,849     | 124,514                | (5,665 )   | (4.5 )%  |
| Segment operating earnings                          | 143,233            | 150,277   | (7,044 )               | (4.7 )%          | 295,555     | 301,436                | (5,881 )   | (2.0 )%  |
| Unallocated expenses and                            | (30,721 )          | (39,175 ) | (8,454 )               | (21.6 )%         | (73,305 )   | (80,202 )              | (6,897 )   | (8.6 )%  |

## restructuring

(a)

|                                            |          |          |          |        |   |           |           |            |        |   |
|--------------------------------------------|----------|----------|----------|--------|---|-----------|-----------|------------|--------|---|
| Consolidated operating earnings            | 112,512  | 111,102  | 1,410    | 1.3    | % | 222,250   | 221,234   | 1,016      | 0.5    | % |
| Interest expense                           | 23,821   | 25,262   | (1,441 ) | (5.7 ) | % | 48,310    | 49,277    | (967 )     | (2.0 ) | % |
| Earnings before provision for income taxes | 88,691   | 85,840   | 2,851    | 3.3    | % | 173,940   | 171,957   | 1,983      | 1.2    | % |
| Provision for income taxes                 | 22,966   | 24,469   | (1,503 ) | (6.1 ) | % | 42,488    | 27,322    | 15,166     | 55.5   | % |
| Net earnings                               | \$65,725 | \$61,371 | \$4,354  | 7.1    | % | \$131,452 | \$144,635 | \$(13,183) | (9.1 ) | % |

## Number of stores at end-of-period

(including franchises):

|              |  |  |  |  |  |       |       |       |        |   |
|--------------|--|--|--|--|--|-------|-------|-------|--------|---|
| SBS          |  |  |  |  |  | 3,718 | 3,782 | (64 ) | (1.7 ) | % |
| BSG          |  |  |  |  |  | 1,388 | 1,393 | (5 )  | (0.4 ) | % |
| Consolidated |  |  |  |  |  | 5,106 | 5,175 | (69 ) | (1.3 ) | % |

## Same store sales growth

(decline) (b)

|              |        |   |        |   |     |     |        |   |        |   |     |     |
|--------------|--------|---|--------|---|-----|-----|--------|---|--------|---|-----|-----|
| SBS          | (0.3 ) | % | (1.6 ) | % | 130 | bps | 0.2    | % | (2.1 ) | % | 230 | bps |
| BSG          | (0.9 ) | % | (1.2 ) | % | 30  | bps | (0.7 ) | % | (1.2 ) | % | 50  | bps |
| Consolidated | (0.5 ) | % | (1.4 ) | % | 90  | bps | (0.1 ) | % | (1.8 ) | % | 170 | bps |

(a) Unallocated expenses consist of corporate and shared costs and are included in selling, general and administrative expenses in our consolidated statements of earnings. Restructuring charges relate to the supply chain modernization plan and the 2018 Restructuring Plan.

(b) For the purpose of calculating our same store sales metrics, we compare the current period sales for stores open for 14 months or longer as of the last day of a month with the sales for these stores for the comparable period in the prior fiscal year. Our same store sales are calculated in constant dollars and include e-commerce sales, but do not generally include the sales from stores that have been relocated until 14 months after the relocation. The sales from stores acquired are excluded from our same store sales calculation until 14 months after the acquisition.

## Results of Operations

The Three Months Ended March 31, 2019 compared to the Three Months Ended March 31, 2018

### Net Sales

Consolidated. Consolidated net sales include a negative impact from changes in foreign currency exchange rates of \$10.5 million, or 1.1% of consolidated net sales.

SBS. The decrease in net sales for SBS for the three months ended March 31, 2019, was primarily driven by the negative impact from changes in foreign currency exchange rates of approximately \$9.0 million, lower sales from the net decline in the number of company-operated stores of \$4.4 million and lower same store sales of approximately \$1.9 million.

SBS's experienced lower unit volume resulting from lower customer traffic and the reduction in the number of company-operated stores during the last 12 months. This was partially offset by an increase in average unit prices, resulting from a change in product mix to higher-priced products and a promotional efficiency effort (which reduced promotions which provided 'free' units, such as Buy One, Get One offers).

BSG. The decrease in BSG's net sales for the three months ended March 31, 2019, was primarily driven by lower sales by our distributor sales consultants of \$11.3 million, same store sales of \$1.3 million and the negative impact from changes in foreign currency exchange rates of approximately \$1.6 million.

The decrease in BSG's net sales also reflects a decrease in unit volume, but notwithstanding the impact of incremental sales from the number of company-operated stores opened. This was partially offset by an increase in average unit prices resulting primarily from the introduction of certain third-party brands with higher average unit prices in the preceding 12 months.

### Gross Profit

Consolidated. Consolidated gross profit decreased for the three months ended March 31, 2019, primarily due to lower net sales in both reportable segments and a lower gross margin in BSG.

SBS. SBS's gross profit decreased for the three months ended March 31, 2019, primarily as a result of a lower net sales. SBS's gross margin was flat, but reflected significantly higher gross margins in our U.S. and Canadian operations, offset by weaker gross margins in our European operations.

BSG. BSG's gross profit decreased for the three months ended March 31, 2019, primarily as a result of a lower net sales and lower gross margin. BSG's gross margin decreased primarily by continued challenges attributed to the ongoing merchandising transformation.

### Selling, General and Administrative Expenses

Consolidated. Consolidated selling, general and administrative expenses decreased primarily as a result of lower compensation and compensation-related expenses and a positive impact from changes in foreign currency exchange rates, partially offset by higher facility expenses and higher expenses related to recent upgrades to our information technology systems. Consolidated selling, general and administrative expenses, as a percentage of net sales, decreased 40 basis points to 38.2% for the three months ended March 31, 2019.



SBS. SBS's selling, general and administrative expenses decreased \$4.2 million, or 1.8%, for the three months ended March 31, 2019. This decrease reflects the impact of the 2018 Restructuring Plan, our recently implemented field structure realignment and store labor hour optimization initiatives and a positive impact from changes in foreign currency exchange rate of approximately \$3.9 million. This decrease was partially offset by higher facility expenses of \$2.3 million and the impact of the reduction of an estimated casualty loss related to hurricanes of \$2.0 million during the three months ended March 31, 2018 with no comparable amounts in the current quarter.

BSG. BSG's selling, general and administrative expenses decreased \$6.7 million, or 6.5%, for the three months ended March 31, 2019, primarily as a result of the impact of the 2018 Restructuring Plan and our recently implemented field structure realignment, lower sales commission of \$1.8 million and a positive impact from changes in foreign currency exchange rate of approximately \$0.5 million.

Unallocated. Unallocated selling, general and administrative expenses, which represent certain corporate costs that have not been charged to our reporting segments, increased \$4.1 million, or 12.7%, for the three months ended March 31, 2019. This increase is primarily from unfavorable variances associated with our self-insurance programs, higher expenses related to recent upgrades to our information technology systems and higher professional fees.

#### Restructuring

For the three months ended March 31, 2019, we recognized income of \$5.8 million in connection with the supply chain modernization plan, which included a \$6.6 million gain from selling our secondary headquarters and fulfillment center in Denton, Texas. For the

three months ended March 31, 2018, we incurred restructuring charges of \$6.8 million in connection with the 2018 Restructuring Plan. See Note 15 of the Notes to Condensed Consolidated Financial Statements included in Item 1 of this Quarterly Report for more information about our restructuring plans.

#### Interest Expense

The decrease in interest expense is primarily from a gain on extinguishment of debt of \$0.5 million in connection with the debt tender offer during the three months ended March 31, 2019, compared to a loss on extinguishment of debt of \$0.9 million in connection with the repricing of the term loan B variable-rate tranche for the three months ended March 31, 2018. See “Liquidity and Capital Resources” below for additional information.

#### Provision for Income Taxes

The provision for income taxes was \$23.0 million and \$24.5 million resulting in an effective tax rate of 25.9% and 28.5%, for the three months ended March 31, 2019 and 2018, respectively. The decrease in our effective tax rate was due primarily to a lower federal statutory rate when compared to the prior year as a result of the U.S. Tax Reform. For the fiscal year 2019, our U.S. federal statutory rate will be 21.0% compared to 24.5% for the prior fiscal year.

The Six Months Ended March 31, 2019 compared to the Six Months Ended March 31, 2018

#### Net Sales

Consolidated. Consolidated net sales include a negative impact from changes in foreign currency exchange rates of \$17.3 million, or 0.9% of consolidated net sales.

SBS. The decrease in net sales for SBS for the six months ended March 31, 2019, was driven by the negative impact from changes in foreign currency exchange rates of approximately \$14.5 million and lower net sales from the net decline in the number of company-operated stores of approximately \$7.1 million, partially offset by an increase in SBS same store sales of approximately \$1.9 million.

SBS’s experienced lower unit volume resulting from lower customer traffic and the reduction in the number of company-operated stores during the last 12 months. This was partially offset by an increase in average unit prices, resulting from a change in product mix to higher-priced products and a promotional efficiency effort.

BSG. The decrease in BSG’s net sales for the six months ended March 31, 2019, was driven by lower sales by our distributor sales consultants of \$11.7 million, sales to our franchisees of \$2.2 million, same store sales of approximately \$2.1 million and the negative impact from changes in foreign currency exchange rates of approximately \$3.0 million. This decrease was partially offset by the positive impact from net new company-operated stores of \$3.5 million.

The decrease in BSG’s net sales also reflects a decrease in unit volume, but notwithstanding the impact of incremental sales from the number of company-operated stores opened. This was partially offset by an increase in average unit prices resulting primarily from the introduction of certain third-party brands with higher average unit prices in the preceding 12 months.

#### Gross Profit

Consolidated. Consolidated gross profit decreased for the six months ended March 31, 2019, primarily due to lower net sales in both reportable segments and a lower gross margin in BSG.

SBS. SBS's gross profit decreased for the six months ended March 31, 2019, primarily as a result of a lower net sales. SBS's gross margin was flat, but reflected significantly higher gross margins in our U.S. and Canadian operations, offset by weaker gross margins in our European operations.

BSG. BSG's gross profit decreased for the six months ended March 31, 2019, primarily as a result of lower net sales and a lower gross margin. BSG's gross margin decreased primarily by continued challenges attributed to the ongoing merchandising transformation.

#### Selling, General and Administrative Expenses

Consolidated. Consolidated selling, general and administrative expenses decreased primarily as a result of lower compensation and compensation-related expenses, lower advertising expenses and a positive impact from changes in foreign currency exchange rates. This decrease was partially offset by increases in facility expenses and recent upgrades to our information technology systems. Consolidated selling, general and administrative expenses, as a percentage of net sales, increased 10 basis points to 37.6% for the six months ended March 31, 2019.

SBS. SBS's selling, general and administrative expenses decreased \$10.2 million, or 2.2%, for the six months ended March 31, 2019. This decrease reflects the impact of the 2018 Restructuring Plan, our recently implemented field structure realignment and store labor hour optimization initiatives, lower advertising expenses of \$1.8 million, a positive impact from changes in foreign currency exchange rate of approximately \$6.1 million. This decrease was partially offset by higher facility expenses of \$4.0 million and the impact of the

reduction of an estimated casualty loss related to hurricanes of \$1.7 million during the six months ended March 31, 2018, with no comparable amounts in the current quarter.

BSG. BSG's selling, general and administrative expenses decreased \$7.9 million, or 3.8%, for the six months ended March 31, 2019, primarily as a result of the impact of the 2018 Restructuring Plan, lower sales commission of \$2.4 million and a positive impact from changes in foreign currency exchange rate of approximately \$0.9 million.

Unallocated. Unallocated selling, general and administrative expenses, which represent certain corporate costs that have not been charged to our reporting segments, increased \$6.9 million, or 10.1%, for the six months ended March 31, 2019. This increase is primarily from unfavorable variances associated with our self-insurance programs, higher expenses related to recent upgrades to our information technology systems and higher professional fees.

### Restructuring

For the six months ended March 31, 2019, we recognized income of \$1.8 million in connection with the supply chain modernization plan, which included a \$6.6 million gain from selling our secondary headquarters and fulfillment center in Denton, Texas, and the 2018 Restructuring Plan. For the six months ended March 31, 2018, we incurred restructuring charges of \$12.0 million in connection with the 2018 Restructuring Plan. See Note 15 of the Notes to Condensed Consolidated Financial Statements included in Item 1 of this Quarterly Report for more information about our restructuring plans.

### Interest Expense

The decrease in interest expense is primarily from a gain on extinguishment of debt of \$0.5 million in connection with the debt tender offer during the six months ended March 31, 2019, compared to a loss on extinguishment of debt of \$0.9 million in connection with the repricing of the term loan B variable-rate tranche during the six months ended March 31, 2018. This decrease was partially offset by higher interest rates on our term loan B variable tranche. See "Liquidity and Capital Resources" below for additional information.

### Provision for Income Taxes

The provision for income taxes was \$42.5 million and \$27.3 million resulting in an effective tax rate of 24.4% and 15.9%, for the six months ended March 31, 2019 and 2018, respectively. The increase in our effective tax rate was due primarily to the impact of the U.S. Tax Reform during the six months ended March 31, 2018. See Note 12 of the Notes to Condensed Consolidated Financial Statements included in Item 1 of this Quarterly Report for more information about the impact of U.S. Tax Reform on our condensed consolidated financial statements.

### Liquidity and Capital Resources

We are highly leveraged and a substantial portion of our liquidity needs will arise from debt service on our outstanding indebtedness and from funding the costs of operations, working capital, capital expenditures, debt repayment and share repurchases. Working capital (current assets less current liabilities) increased \$89.5 million, to \$753.4 million at March 31, 2019, compared to \$663.9 million at September 30, 2018, resulting primarily from increases in cash and cash equivalents and inventory, and from decreases in accounts payable and accrued liabilities.

At March 31, 2019, cash and cash equivalents were \$89.8 million. Based upon the current level of operations and anticipated growth, we anticipate that existing cash balances (excluding certain amounts permanently invested in connection with foreign operations), funds expected to be generated by operations and funds available under the ABL facility will be sufficient to meet working capital requirements, potential acquisitions, finance anticipated capital

expenditures, including information technology upgrades and store remodels, debt repayments and opportunistic share repurchases over the next 12 months. For the foreseeable future, we will prioritize needed investments in our business that we believe will deliver value for stockholders, then focus on measured debt repayment within our ratings guidance and then share repurchases.

We utilize our ABL facility for the issuance of letters of credit, for certain working capital and liquidity needs and to manage normal fluctuations in our operational cash flow. In that regard, we may from time to time draw funds under the ABL facility for general corporate purposes including funding of capital expenditures, acquisitions, interest payments due on our indebtedness, paying down other debt and opportunistic share repurchases. During the six months ended March 31, 2019, the weighted average interest rate on our borrowings under the ABL facility was 5.2%. The amounts drawn are generally paid down with cash provided by our operating activities. As of March 31, 2019, Sally Holdings had \$481.9 million available for borrowings under the ABL facility, subject to borrowing base limitations, as reduced by outstanding letters of credit.

#### Share Repurchase Programs

We did not repurchase any shares of our common stock during the six months ended March 31, 2019. As of March 31, 2019, we had authorization of approximately \$834.1 million of additional potential share repurchases remaining under the 2017 Share Repurchase Program. During the six months ended March 31, 2018, we repurchased and subsequently retired approximately 6.7 million shares of

our common stock under Board approved share repurchase programs at an aggregate cost of \$114.5 million. We funded these share repurchases with existing cash balances, cash from operations and borrowings under the ABL facility.

#### Historical Cash Flows

Historically, our primary source of cash has been net funds provided by operating activities and, when necessary, borrowings under our ABL facility. The primary uses of cash have been for share repurchases, capital expenditures, repayments and servicing of long-term debt and acquisitions.

#### Net Cash Provided by Operating Activities

Net cash provided by operating activities during the six months ended March 31, 2019, decreased \$69.3 million to \$110.1 million, compared to the six months ended March 31, 2018, mainly due to a focused reduction of accounts payable and an increase in inventory as a result of the launch of new product lines.

#### Net Cash Used by Investing Activities

Net cash used by investing activities during the six months ended March 31, 2019, decreased \$10.6 million to \$37.2 million, compared to the six months ended March 31, 2018. This change was primarily driven by cash proceeds received from selling our secondary headquarters and fulfillment center in Denton, Texas, and as a result of not having any significant acquisitions in the six months ended March 31, 2019, partially offset by the additional capital expenditures primarily from investments in our information technology systems.

#### Net Cash Used by Financing Activities

Net cash used by financing activities during the six months ended March 31, 2019, decreased \$68.1 million to \$59.9 million, compared to the six months ended March 31, 2018. This decrease was driven by a focus on debt reduction rather than share repurchases.

#### Long-Term Debt

At March 31, 2019, we had \$1,731.7 million in debt, not including capital leases, unamortized debt issuance costs or debt discounts, in the aggregate, of \$17.8 million. Our debt consisted of \$889.9 million of senior notes outstanding and a term loan B with an outstanding principal balance of \$836.3 million. There were no borrowings outstanding under our ABL facility as of March 31, 2019.

During the three months ended March 31, 2019, we repurchased approximately \$60.1 million aggregate principal amount of our 2025 Notes and our 2023 Notes in a debt tender offer at a price of 98.0% and 100.0%, respectively, excluding accrued interest.

We are currently in compliance with the agreements and instruments governing our debt, including our financial covenants.

#### Contractual Obligations

There have been no material changes outside the ordinary course of our business in any of our contractual obligations since September 30, 2018.

#### Off-Balance Sheet Financing Arrangements

At March 31, 2019 and September 30, 2018, we had no off-balance sheet financing arrangements other than operating leases incurred in the ordinary course of our business, and outstanding letters of credit related to inventory purchases and self-insurance programs.

#### Critical Accounting Estimates

There have been no material changes to our critical accounting estimates or assumptions since September 30, 2018.

#### Accounting Changes and Recent Accounting Pronouncements

See Note 3 of the Notes to Condensed Consolidated Financial Statements in Item 1 – “Financial Statements” in Part I – Financial Information.

#### Item 3. Quantitative and Qualitative Disclosures About Market Risk

As a multinational corporation, we are subject to certain market risks including foreign currency fluctuations, interest rates and government actions. There have been no material changes to our market risks from September 30, 2018. See our disclosures about market risks contained in Item 7A. “Quantitative and Qualitative Disclosures about Market Risk” in Part II of our Annual Report on Form 10-K for the fiscal year ended September 30, 2018

#### Item 4. Controls and Procedures

**Controls Evaluation and Related CEO and CFO Certifications.** Our management, with the participation of our principal executive officer (“CEO”) and principal financial officer (“CFO”), conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of March 31, 2019. The controls evaluation was conducted by our Disclosure Committee, comprised of senior representatives from our finance, accounting, internal audit, and legal departments under the supervision of our CEO and CFO.

Certifications of our CEO and our CFO, which are required in accordance with Rule 13a-14 of the Exchange Act, are attached as exhibits to this Quarterly Report. This “Controls and Procedures” section includes the information concerning the controls evaluation referred to in the certifications and it should be read in conjunction with the certifications for a more complete understanding of the topics presented.

**Limitations on the Effectiveness of Controls.** We do not expect that our disclosure controls and procedures will prevent all errors and all fraud. A system of controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the system are met. Because of the limitations in all such systems, no evaluation can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. Furthermore, the design of any system of controls and procedures is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how unlikely. Because of these inherent limitations in a cost-effective system of controls and procedures, misstatements or omissions due to error or fraud may occur and not be detected.

**Scope of the Controls Evaluation.** The evaluation of our disclosure controls and procedures included a review of their objectives and design, our implementation of the controls and procedures and the effect of the controls and procedures on the information generated for use in this Quarterly Report. In the course of the evaluation, we sought to identify whether we had any data errors, control problems or acts of fraud and to confirm that appropriate corrective action, including process improvements, was being undertaken if needed. This type of evaluation is performed on a quarterly basis so that conclusions concerning the effectiveness of our disclosure controls and procedures can be reported in our Quarterly Reports on Form 10-Q and our Annual Reports on Form 10-K. Many of the components of our disclosure controls and procedures are also evaluated by our internal audit department, by our legal department and by personnel in our finance organization. The overall goals of these various evaluation activities are to monitor our disclosure controls and procedures on an ongoing basis and to maintain them as dynamic systems that change as conditions warrant.

**Conclusions regarding Disclosure Controls.** Based on the required evaluation of our disclosure controls and procedures, our CEO and CFO have concluded that, as of March 31, 2019, we maintain disclosure controls and procedures that are effective in providing reasonable assurance that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms, and that such information is accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

**Changes in Internal Control over Financial Reporting.** During our most recent fiscal quarter, there have been no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.



## PART II — OTHER INFORMATION

### Item 1. Legal Proceedings

We are involved, from time to time, in various claims and lawsuits incidental to the conduct of our business in the ordinary course. We carry insurance coverage in such amounts in excess of our self-insured retention as we believe to be reasonable under the circumstances and that may or may not cover any or all of our liabilities in respect of these matters. We do not believe that the ultimate resolution of these matters will have a material adverse impact on our consolidated financial position, cash flows or results of operations.

We are subject to a number of U.S., federal, state and local laws and regulations, as well as the laws and regulations applicable in each foreign country or jurisdiction in which we do business. These laws and regulations govern, among other things, the composition, packaging, labeling and safety of the products we sell, the methods we use to sell these products and the methods we use to import these products. We believe that we are in material compliance with such laws and regulations, although no assurance can be provided that this will remain true going forward.

See also Note 16 of the Notes to Condensed Consolidated Financial Statements included in Item 1 of this Quarterly Report.

### Item 1A. Risk Factors

In addition to the other information set forth in this Quarterly Report, you should carefully consider the factors contained in Item 1A. “Risk Factors” in Part I of our Annual Report on Form 10-K for the fiscal year ended September 30, 2018, which could materially affect our business, financial condition or future results. There have been no material changes from the risk factors disclosed in such Annual Report. The risks described in such Annual Report and herein are not the only risks facing our company.

Item 6. Exhibits

Exhibit No. Description

- 3.1 Third Restated Certificate of Incorporation of Sally Beauty Holdings, Inc., dated January 30, 2014, which is incorporated herein by reference from Exhibit 3.3 to the Company's Current Report on Form 8-K filed on January 30, 2014
- 3.2 Amended and Restated Bylaws of Sally Beauty Holdings, Inc., dated April 26, 2017, which is incorporated herein by reference from Exhibit 3.1 to the Company's Current Report on Form 8-K filed on April 28, 2017
- 31.1 Rule 13a-14(a)/15d-14(a) Certification of Christian A. Brickman\*
- 31.2 Rule 13a-14(a)/15d-14(a) Certification of Aaron E. Alt\*
- 32.1 Section 1350 Certification of Christian A. Brickman\*
- 32.2 Section 1350 Certification of Aaron E. Alt\*
- 101 The following financial information from our Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2019, formatted in XBRL (Extensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets; (ii) the Condensed Consolidated Statements of Earnings; (iii) the Condensed Consolidated Statements of Comprehensive Income; (iv) the Condensed Consolidated Statements of Cash Flows; (v) the Condensed Consolidated Statements of Stockholders' Deficits; and (vi) the Notes to Condensed Consolidated Financial Statements.

\* Included herewith

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SALLY BEAUTY HOLDINGS, INC.  
(Registrant)

Date: May 1, 2019

By: /s/ Aaron E. Alt  
Aaron E. Alt  
Senior Vice President, Chief Financial Officer

and President – Sally Beauty Supply  
For the Registrant and as its Principal Financial Officer