

# **Lululemon athletica inc. to Acquire Home Fitness Innovator MIRROR**

## **Company Participants**

- Calvin McDonald, Chief Executive Officer
- Howard Tubin, Vice President of Investor Relations
- Meghan Frank, Senior Vice President of Financial Planning and Analysis

## **Other Participants**

- Adrienne Yi, Analyst, Barclays
- Erinn Murphy, Analyst, Piper Jaffray
- Mark Altschwager, Analyst, Baird
- Matt McClintock, Analyst, Raymond James
- Omar Saad, Analyst, Evercore ISI

## **Presentation**

### **Operator**

Thank you for standing by. This is the conference operator. Welcome to the Lululemon Athletica, Inc. Lululemon to acquire MIRROR Conference call. As a reminder, all participants are in listen-only mode and the conference is being recorded. After the presentation, there will be an opportunity to ask questions. (Operator Instructions) I would now like to turn the conference over to Mr. Howard Tubin, Vice President of Investor Relations for Lululemon Athletica, Inc. Please go ahead sir.

### **Howard Tubin {BIO 6382352 <GO>}**

Thank you and good afternoon. Welcome to our conference call to announcing our acquisition of MIRROR. Joining me today are Calvin McDonald, CEO; Meghan Frank, SVP of Financial Planning and Analysis; and Alex Grieve, VP and Controller. Before we get started, I'd like to take this opportunity to remind you that our remarks today will include forward-looking statements reflecting management's current forecast of certain aspects of Lululemon's future. These statements are based on current information, which we have assessed which by its nature is dynamic and subject to rapid and even abrupt changes. Actual results may differ materially from those contained in or implied by these forward-looking statements due to risks and uncertainties associated with our business.

Including those we have disclosed in our most recent filings with the SEC, including our annual report on Form 10-K and our quarterly reports on Form 10-Q. Any

forward-looking statements that we make on this call are based on assumptions as of today and we expressly disclaim any obligation or undertaking to update or revise any of these statements as a result of new information or future events. Before we begin, I'd like to point you to our -- the Investor section of our website [www.lululemon.com](http://www.lululemon.com) where we posted a slide deck that we'll be referring to during the call. Today's call is scheduled for approximately 30 minutes, so please limit yourself to one question at a time to give others the opportunity to have their questions addressed. And now, I'd like to turn the call over to Calvin.

**Calvin McDonald** {BIO 16657186 <GO>}

Thank you, Howard and thank you all for joining us on short notice. I hope, you had a chance to read the press release and download the slide deck from our Investor site and I appreciate the opportunity to provide some additional details about Lululemon's acquisition of MIRROR. I'll walk you through the slides. Now, let's start on Slide 3. Let me begin by sharing these thoughts about the announcement today and what it signals for the future and why it has been so compelling to all of us. There is something special about Lululemon, a well-informed intuition. We listen deeply to our guests, ambassadors and our collective. We've developed our five-year vision and strategy, understanding the future and the opportunity to integrate both digital and physical experiences, recognize the power of versatile sweat activities and bring together physical, social and emotional health. Our five-year strategic road map was built around these premises. We invested in this future through omni experiences, our partnership with MIRROR in 2019, digital sweat offerings and our dynamic channel infrastructure. We are seeing these trends accelerate to create a structure change and we're ready. MIRROR is an important step in our strategy in creating the future of the sweat life. With this grounding, I'd like to introduce you to MIRROR. On Slide 4, you'll see the details around MIRROR. I know, we've spoken about MIRROR during some of our earnings call since our initial investment in 2019.

Founded in 2016 and launched in 2018 by our former Lululemon ambassador, Brynn Putnam, they remain in the early stages of their life cycle. They have grown incredibly fast in just two years with so much runway ahead giving the expanding home fitness market and our acquisition enables us to significantly raise the awareness of MIRROR as they become part of the Lululemon's family. MIRROR has an appealing business model, which includes revenue streams from both the sale of its proprietary device and also a content offering via an ongoing subscription model. And they compete in the \$500 billion market for global physical activity, a large and rapidly growing subset of the 3 trillion market for global wellness.

They're known for innovative at home interactive fitness studio experiences that combine both the screen and a mirror to deliver live and on-demand sweat content while at the same time allowing the user to see their physical form. Versatile fitness and activity offerings with weekly live classes and thousands of on-demand workouts as well as immersive one on one personal training. Workouts range from boxing to boot camp to yoga and meditation. Energized community and influencer buzz, very strong guest loyalty, which is very similar to what we have at Lululemon and powerful and scalable content platform. It's US-based today with opportunity to expand in

North America and around the world. And what are they doing well? MIRROR operates a lean and efficient model and generates the vast majority of their sales through its website mirror.co. They also offer compelling value proposition compared to other fitness hardware that is limited to a single discipline and very strong online channel sales and marketing. The Lululemon and MIRROR partnership, as I mentioned, MIRROR CEO, Brynn was a Lululemon ambassador in New York, which created a foundation for our partnership from the beginning. We made an initial investment in MIRROR in mid-2019, which has allowed us to see the synergies between our brands. Earlier this year, MIRROR launched a new meditation content vertical with Lululemon global ambassador, Gabby Bernstein. Other ambassadors have also launched content on MIRROR recently including our long time ambassador, Baron Baptiste. These are just some of the reasons that this is an ideal first acquisition for Lululemon with an incredible growth opportunity going forward.

On Slide 5, we share some of the key stats with you and some of the successes by the numbers. As you can see, since launching in 2018, very impressive growth. These numbers start to show the opportunity for scale as part of Lululemon. \$100 million plus in revenues expected for 2020, a 50% split between female and male demographics, 70-plus new classes per week, 40 plus types of different classes and only 10% today are actually familiar with the products, so the potential around driving awareness and consideration is significant. In the bottom of this page, you can see the trend line for their search growth, which has accelerated at the beginning of the year and continued as COVID-19 increase the importance of in-home fitness. Beyond these impressive details, let me also provide insights into why this is the right acquisition at the right time.

On Slide 6, I'll share with you the same vision that we shared last year during Analysts Day. The MIRROR brand naturally folds into our vision, which I shared at that point. Our vision is to be the experiential brand that ignites a community of people living the sweat life through sweat, grow and connect. On Slide 7, at that same time I shared with you our 2023 five-year growth plan to achieve our vision, called The Power of Three, which is comprised of three pillars. Innovative products with growth in our core product categories and doubling our men's business, omni guest experiences with expansion through experiential stores in our membership program, our agile store formats and our digital growth, which would double in five years and expanding markets with continued growth in our core market of North America and meaningfully more growth in international markets led by China, which we expect to quadruple in five years. We remain committed to these growth targets and we are confident in our ability to navigate the near-term challenges of COVID-19 while we continue to invest in our future. And that's where today's announcement fits in nicely. Although, building on our power of three strategy, we do not need the acquisition to achieve our 23 goals. This initiative would be incremental to the five-year numbers we shared with you. The next slide details our strategic roadmap to support this pillar. We have been identifying and implementing ways to enhance our digital sweat life offering for at least the past year. We made the initial investment in partner with MIRROR 12 months ago, studied and learned the business from the inside and decided to pursue this opportunity.

Even prior to COVID-19, digital has been enabling new experiences and behaviors within the sweat life ecosystem. COVID-19 accelerated an already emerging trend. Our strategy is based upon digital content is changing, how and where our guests sweat, grow and connect. Pre-COVID, 64% of our guests utilized an at home digital sweat option. COVID phase, 75% of our guests utilized an at home digital sweat option and post-COVID, 86% of those with at home equipment say they will use at home digital sweat the same or more as they had been using prior to COVID-19. Digital content is changing and studio and trainer models for our ambassadors are changing with that.

With this, we have more opportunities online with experiences that created community feel through the digital environment. Our omni strategy is rooted in supporting our community vision to foster connection among people in the practice of the sweat life inspired by our ambassadors in a seamless physical and digital journey, scale the sweat life to reach more of our guests and future guests with the power of community, bolster our competitive advantage to modernize our grassroots marketing and to accelerate membership growth, integrated digital solution to enable even faster expansion.

The next slide details the ecosystem that we're creating and supports this acquisition. The MIRROR platform provides a versatile and immersive in home sweat solution that will leverage the powerful Lululemon ecosystem, including community, the MIRROR gains access to our guests in collective, made up of our guests and members, the physical infrastructure. MIRROR can be used to further connect the physical through events, experiential stores, local studios, ambassadors. MIRROR gains access to our ambassadors for content creation and opening curated platform. MIRROR gains are trusted lens of curation, and we gain the versatile and immersive hardware in home and that's a compelling combination. A place in the home, daily mindshare and a platform for ambassadors. And that is where the synergy just begins. On the next slide, we place the synergies between Lululemon and MIRROR side by side, this combination between Lululemon and MIRROR will provide meaningful synergies to both our businesses. What we bring to MIRROR is access to our large growing and loyal guests, leverage distribution channels to scale growth, utilize marketing channels to lower guest acquisition costs, expand talent through our unique ambassador community, reduce consideration barriers with strong brand credibility and lead generation from our most engaged guests.

What MIRROR can bring to Lululemon, expand and innovate our omni guest experiences, dynamic platform to enhance and scale the guest offerings, accelerate monetization of digital sweat, create immediate revenue stream with the path to profitability, amplify Lululemon ambassadors and creates community and establishes product integration opportunities. The next page provides the financial details. Meghan Frank is joining me on the call for Q&A along with Alex and can answer any questions you may have on the financials. But let me just highlight the following.

The purchase price is \$500 million. We will finance the transaction from our \$1.5 billion of liquidity, which includes over \$800 million in cash, our existing \$400 million revolver and a new one year \$300 million revolver and the transaction will

close in the next one to two weeks. On the final slide, I'd like to summarize what makes this acquisition so compelling. And in conclusion, let me summarize what makes us so excited about moving forward with MIRROR.

First, MIRROR brings a content platform that connects our sweat life ecosystem and integrates our strong assets. Second, MIRROR allows us to offer new omni experiences to our guests and support them to live the sweat life in many new ways. Third, Lululemon can bring significant awareness to MIRROR through our marketing and distribution channels, help them grow and reduce customer acquisition costs. Fourth, our vision and Power of Three plan has not changed. MIRROR growth adds to the potential. And finally, with the financial strength and liquidity to complete this transaction and continue to run our business day to day and plan for contingencies. Thank you for joining us today. As you can see, there are many considerations that made this acquisition an ideal opportunity for both Lululemon and MIRROR as well as the guest and members of both brands, and I look forward to answering your questions.

## Questions And Answers

### Operator

Thank you. We will now begin the question-and-answer session. (Operator Instructions) The first question comes from Erinn Murphy from Piper Sandler. Please go ahead.

### Q - Erinn Murphy {BIO 17718258 <GO>}

Great, thanks, good afternoon. I guess a couple of questions from me. First, just maybe on the path to profitability of MIRROR. I would love to hear kind of they integrate with you guys, how that looks and then maybe a couple for Meghan. Sorry if I missed this. What was the existing -- what is the existing user base of MIRROR. And then what was revenue in 2019? I'm assuming 2020 plan to get \$200 million plus was clearly enabled by what we've seen in this digital transformation this year. Thank you.

### A - Meghan Frank {BIO 21694519 <GO>}

Yeah, hi Erinn, it's Meghan. So in terms of the path to profitability, what we are -- what we disclosed was that they will be modestly dilutive to our EPS for the full year of 2020 and that's excluding deal related costs. And then they will be modestly accretive in 2021 again excluding deal related costs. When we look beyond that, I think it's a little bit too early to share our thinking as we move into the integration phase. So we'll come back on that when we revert back to providing guidance for 2021 and beyond. And then in terms of existing user base, we aren't going to be sharing any metrics around that. I'd say, outside of program, subscription sales, the key metrics that we looked at as we looked at the deal were around retention, member engagement and satisfaction and we were pleased with the strength we saw in those metrics as we completed our process.

**Q - Erinn Murphy** {BIO 17718258 <GO>}

Got it. And then I'm sorry, the revenue in 2019. Can you share that with us?

**A - Meghan Frank** {BIO 21694519 <GO>}

In terms of revenue in 2019, we are going to be showing the specifics now.

**Q - Erinn Murphy** {BIO 17718258 <GO>}

Okay, thank you. Fair enough.

**Operator**

Thank you. The next question comes from Matt McClintock from Raymond James. Please go ahead.

**Q - Matt McClintock** {BIO 16452505 <GO>}

Hi, yes, everyone. So I guess two questions, the first one is, it sounds like the way that you're approaching this from a financial model perspective is MIRROR as a standalone investment, it can generate revenue, it can generate profit and at the same time, it helps with acquisition -- customer acquisitions. Can you at least elaborate a little bit more in terms of the ability to sell product, Lululemon product, is that in any way in consideration of this acquisition meaning being able to use MIRROR to sell Lululemon outside of just being able to use MIRROR to drive broader brand awareness of the Lululemon brand, just can you dig a little bit more just actually selling products? Thanks.

**A - Calvin McDonald** {BIO 16657186 <GO>}

Yeah, absolutely, Matt. It's Calvin, when we look at the opportunities, what I loved about MIRROR was as you led, it's a standalone business that is going to drive very good revenue growth. Would be profitable. We'll be able to connect to our membership plan and program to accelerate both of those and they will over the coming years be a meaningful driver of our collective growth. In addition to that the fact that we are going to be building on our community, which we know today drives loyalty the fact that we will have a place in the home, have daily mindshare, guest interacting with the brand with a sweat ambassadors and instructors wearing Lululemon, which is where the brand built a lot of the momentum early on with grassroots marketing in the communities, having that opportunity as well as additional initiatives that we've talked about of how we introduce product to the guests using this platform in the house is incremental and absolutely something, we considered and we'll look to innovate and pursue. But as just a stand-alone, it's a meaningful -- will be a meaningful business and our ability to connect the two and into contributing to driving more apparel sales is absolutely something we've considered but it wasn't the primary thesis behind the investment which to me is just another level of incremental growth driving loyalty and daily mind share with the guest which by the way over the last few months, we've learned since our community initiatives and sweat is a huge advantage for our brand that guests are interacting and thinking of Lululemon not just for a transaction in need that they're interacting

with the brand on an ongoing daily basis and this just reinforces and it allows us to be in that discussion, which will have and we've seen it -- a positive impact on apparel sales.

**Q - Matt McClintock** {BIO 16452505 <GO>}

Thanks for that Calvin and then just as a follow-up. I hate to ask this but in the fourth quarter, you made the statement that you were prepared to make investments and use your strong competitive position to make investments and this is clearly example of that, but I have to ask just liquidity making such a sizable investment during this time. How do you think through that? How does that play into your calculus given that there is constant fears that there might be a second wave of Coronavirus coming through? Thank you.

**A - Calvin McDonald** {BIO 16657186 <GO>}

Yeah. No, absolutely Matt. A couple of things, one as we shared in our quarter one this year although our operations was impacted, we were able to still generate a profit. We shared with you the momentum that's happening in the business, both globally as well as in North America as stores open and we've continued to see triple-digit growth in our online business. There is strong demand for our product. We are servicing that demand through our stores that have opened and continue on online with quite strong growth and we've modeled a variety of scenarios. We're open everywhere, but New York, we closed Houston. When we close stores now, we still default to a BBR position as well as curbside pickup or buy online pickup at door so even a default close position isn't what it was earlier in April.

So we modeled a variety of scenarios, both with the North America, the globe and feel very, very confident in the liquidity of the business and we've added \$300 million in additional credit facility, which gives us \$1.5 billion at our disposal. So we feel very good and have modeled a variety of scenarios and felt good about the acquisition at this time.

**Q - Matt McClintock** {BIO 16452505 <GO>}

Thank you for that. I'm buying my MIRROR tonight. Thanks.

**A - Calvin McDonald** {BIO 16657186 <GO>}

Great.

**Operator**

Your next question comes from Adrienne Yi from Barclays. Please go ahead.

**Q - Adrienne Yi** {BIO 22704408 <GO>}

Yes, good afternoon and congratulations. Calvin, I was wondering if you had talked about the \$500 billion, physical fitness, but I think that you're talking about the more -- more broadly. I was wondering if you can help us kind of dig into the component that is digital Connected Fitness and then also the opportunity with the physical

infrastructure. If you could help us with that as well. How big is that potentially part of the business and when would that be more aggressively rolled out? Thank you very much.

**A - Calvin McDonald** {BIO 16657186 <GO>}

No, absolutely. I'll talk and I'll leave -- Meghan, in terms of the size of the market, we sort of share the \$500 billion addressable market opportunity and I think there is a variety of ways we can define it within that number. We know that at home is evolving, at home through these subscription models are evolving and growing exponentially. So we see the size and potential behind this space is being very dramatic, what we get excited about when we think of the integration into our physical space is one, selling obviously MIRROR on lululemon.com, we're going to be testing in the back half, selling it in a number of doors learning and being able to roll that out. Once you see MIRROR, once you see the platform, the fact that you only need one in store to display it, the fact that we already have the logistics and the technology to do BBR where guests are ordering in store and having it shipped to their house, we already have that behavior inside the organization.

So from an efficiency standpoint, we are very effective to be able to offer that and then as we've built out and thought about it through our experiential stores through our events and our ambassador community, how we leverage the platform to support those, how we think of a network of experiential stores where we can be filming live classes to produce content for MIRROR. The synergies again, what we appreciated about MIRROR and the growth that they've achieved so far, which is very significant considering the opportunity and awareness behind the brand is predominantly done through online.

They have two physical locations and the rest of their business has been grown online, which is one of the reasons why their profitability model is going to tip profitable I think quicker than some other models out there, but our ability to bring that into the physical drive awareness, tap into our online and leverage our network is a big part of the vision that we have in building out the ecosystem.

**Q - Adrienne Yi** {BIO 22704408 <GO>}

Great. Thank you. And the physical infrastructure?

**A - Meghan Frank** {BIO 21694519 <GO>}

Physical infrastructure, Adrienne, do you mean by store?

**Q - Adrienne Yi** {BIO 22704408 <GO>}

No the market opportunity for that?

**A - Meghan Frank** {BIO 21694519 <GO>}

So I think, right now, the business is only in the US and we plan to expand our stores and start to test and learn in Q4 and I think beyond that we see opportunities in our



international markets as we expand into additional doors. And we'll certainly come back and share more as our plans evolve as we get further into integration.

**Q - Adrienne Yi** {BIO 22704408 <GO>}

Great, thank you very much.

## **Operator**

Your next question comes from Omar Saad from Evercore ISI. Please go ahead.

**Q - Omar Saad** {BIO 5302683 <GO>}

Thanks for taking my question. Fascinating acquisition. We've seen kind of a mixed track record of athletic brands getting into the IT hardware space or buying platforms, but it seems very opportunistic, Calvin. Isn't the way to think about this is a small company with a great product and service that's very synergistic with your vast legions of guests and consumer faithfuls that you can introduce this brand to potentially million -- this product and service to millions of new customers, is that the right way to think about it? And in every Lulu store eventually, if everything goes as according to plan?

**A - Calvin McDonald** {BIO 16657186 <GO>}

Hey, Omar. I think that is one of the lead ways to look at the acquisition. What we liked about it compared to other acquisitions that have been made in this space is it is a revenue driver. It has the recurring revenue of a subscription model. The guest is purchasing a product and what immediately Lululemon can bring is awareness, channel distribution at a very low cost and drive unit sales, which will drive that reoccurring model of subscription then you layer in the content that we can bring through our vast ambassador community globally, 2000 plus ambassadors not to mention our global, our legacy ambassadors then you roll in our store network and experiential stores to be able to create hubs, where we can continue to enrich that content or the additional of events. I mean, content, we're going to enrich but outside of all of that they make money today, guests buy a product and use a product and we're excited about that.

The point that we can sell and have the potential to sell even more apparel through the loyalty and building loyalty with our guests and expand that is completely incremental to the investment thesis and what needs to happen, and I think that's where some of the other ones are challenged when it's you're acquiring the ability or the opportunity to then convert to a sale. This is a sale and it's a proven sale and we're going to bring awareness and consideration that will drive it and as we build out, integrate that ecosystem and community. I think, it will layer in more opportunity for us going forward. That's the right way to look at it.

**Q - Omar Saad** {BIO 5302683 <GO>}

Understood. You've been engaged with them for a couple of years already. Was this kind of always in the works or did COVID change the nature of the relationship?

**A - Calvin McDonald** {BIO 16657186 <GO>}

No, it's, I would say what's been one year we've been in relationship. We've been in relationship with Brynn going back with her being a legacy ambassador. We started the relationship, a year ago. It's always been a space that I've been very interested in. It absolutely supports and builds upon our exciting vision and we've test and learned leading into COVID and I would say the opportunity of COVID is that it's brought the future closer to the present and we were able to see the power of in-home sweat, the power of community, the ecosystem, the adoption by guests and really the potential that we have around driving awareness and consideration and through our own channels, the way the guest was interacting with our brand, our ambassador community through a variety of digital sites being able to offer that on an ongoing basis through that. So it was in the works and it clearly accelerated our learning and the potential and guest adoption sooner.

**Q - Omar Saad** {BIO 5302683 <GO>}

Thank you.

**A - Meghan Frank** {BIO 21694519 <GO>}

Operator, we'll take one more question, please.

**Operator**

Certainly, sir. The next question comes from Mark Altschwager from Baird. Please go ahead.

**Q - Mark Altschwager** {BIO 18088928 <GO>}

Good afternoon. Thanks for taking my question. Could you just speak a bit more about how we should think about the ongoing investment in contents for MIRROR, especially as you integrate more with the Lululemon ambassadors?

**A - Calvin McDonald** {BIO 16657186 <GO>}

Hey Mark, investment from a dollar perspective or from a strategy perspective?

**Q - Mark Altschwager** {BIO 18088928 <GO>}

More from a dollar perspective.

**A - Calvin McDonald** {BIO 16657186 <GO>}

Yeah, well, again, I would not model or view any significant change in our need to leverage the ambassador community and create the opportunity for them on the platform. MIRROR has a very efficient operating model when compared to others. And we don't see that changing meaningfully and our relationship with our ambassadors already sort of allows us to utilize them in this particular manner and leverage on this platform if they're equally excited about it. So we're excited about

the potential and leveraging our broad network of ambassadors. And we don't see a meaningful change to the model that MIRROR has already established.

**Q - Mark Altschwager** {BIO 18088928 <GO>}

That's helpful. And then one last real quick one. I'm curious if you know what percentage of MIRROR's subscribers are active Lululemon customers?

**A - Meghan Frank** {BIO 21694519 <GO>}

So there is approximately a 50% overlap in the customer base between MIRROR and Lululemon, which we view as an opportunity on both sides.

**Q - Mark Altschwager** {BIO 18088928 <GO>}

Thank you.

**Operator**

Thank you. That is all the time we have for questions. Thank you for joining us today and we look forward to speaking with you soon. Goodbye.

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