

lululemon athletica inc.
Form 10-Q
September 09, 2011

Table of Contents

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

Form 10-Q

(Mark One)

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended July 31, 2011
- or
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

Commission file number 001-33608

lululemon athletica inc.

(Exact name of registrant as specified in its charter)

Delaware

*(State or other jurisdiction of
incorporation or organization)*

**400-1818 Cornwall Avenue,
Vancouver, British Columbia**

(Address of principal executive offices)

20-3842867

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

V6J 1C7

(Zip Code)

Registrant's telephone number, including area code:

604-732-6124

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

N/A

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

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

Edgar Filing: lululemon athletica inc. - Form 10-Q

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

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

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

At September 6, 2011, there were 108,803,942 shares of the registrant's common stock, par value \$0.005 per share, outstanding.

Exchangeable and Special Voting Shares:

At September 6, 2011, there were outstanding 34,524,680 exchangeable shares of Lulu Canadian Holding, Inc., a wholly-owned subsidiary of the registrant. Exchangeable shares are exchangeable for an equal number of shares of the registrant's common stock.

In addition, at September 6, 2011, the registrant had outstanding 34,524,680 shares of special voting stock, through which the holders of exchangeable shares of Lulu Canadian Holding, Inc. may exercise their voting rights with respect to the registrant. The special voting stock and the registrant's common stock generally vote together as a single class on all matters on which the common stock is entitled to vote.

TABLE OF CONTENTS

	Page
PART I. FINANCIAL INFORMATION	
Item 1.	FINANCIAL STATEMENTS: 3
	CONSOLIDATED BALANCE SHEETS as of July 31, 2011 and January 30, 2011 3
	CONSOLIDATED STATEMENTS OF OPERATIONS for the thirteen and twenty-six weeks ended July 31, 2011 and August 1, 2010 4
	CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY for the twenty-six weeks ended July 31, 2011 5
	CONSOLIDATED STATEMENTS OF CASH FLOWS for the twenty-six weeks ended July 31, 2011 and August 1, 2010 6
	NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS 7
Item 2.	MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS 13
Item 3.	QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK 26
Item 4.	CONTROLS AND PROCEDURES 26
PART II. OTHER INFORMATION	
Item 1.	LEGAL PROCEEDINGS 27
Item 1A.	RISK FACTORS 27
Item 2.	UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS 35
Item 6.	EXHIBITS 35
	SIGNATURES 36
	<u>EX-31.1</u>
	<u>EX-31.2</u>
	<u>EX-32.1</u>
	<u>EX-101 INSTANCE DOCUMENT</u>
	<u>EX-101 SCHEMA DOCUMENT</u>
	<u>EX-101 CALCULATION LINKBASE DOCUMENT</u>
	<u>EX-101 LABELS LINKBASE DOCUMENT</u>
	<u>EX-101 PRESENTATION LINKBASE DOCUMENT</u>
	<u>EX-101 DEFINITION LINKBASE DOCUMENT</u>

Table of Contents

PART I
FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

lululemon athletica inc. and Subsidiaries

CONSOLIDATED BALANCE SHEETS

	July 31, 2011	January 30, 2011
	(Unaudited)	
	(Amounts in thousands, except per share amounts)	
ASSETS		
Current assets		
Cash and cash equivalents	\$ 264,728	\$ 316,286
Accounts receivable	9,720	9,116
Inventories	88,884	57,469
Prepaid expenses and other current assets	20,640	6,408
	383,972	389,279
Property and equipment, net	151,120	70,954
Goodwill and intangible assets, net	28,434	27,112
Deferred income taxes	18,379	7,894
Other non-current assets	4,556	4,063
	\$ 586,461	\$ 499,302
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities		
Accounts payable	\$ 4,445	\$ 6,659
Accrued liabilities	28,809	25,266
Accrued compensation and related expenses	16,819	16,872
Income taxes payable		18,399
Unredeemed gift card liability	14,885	18,168
	64,958	85,364
Non-current liabilities	21,826	19,645
	86,784	105,009
Stockholders equity		

Edgar Filing: lululemon athletica inc. - Form 10-Q

Undesignated preferred stock, \$0.01 par value, 5,000 shares authorized, none issued and outstanding		
Exchangeable stock, no par value, 60,000 shares authorized, issued and outstanding 34,525 and 35,636		
Special voting stock, \$0.000005 par value, 60,000 shares authorized, issued and outstanding 34,525 and 35,636		
Common stock, \$0.005 par value, 400,000 shares authorized, issued and outstanding 108,773 and 106,756	544	534
Additional paid-in capital	197,022	179,870
Retained earnings	261,407	189,656
Accumulated other comprehensive income	36,416	20,329
	495,389	390,389
Non-controlling interest	4,288	3,904
	\$ 586,461	\$ 499,302

See accompanying notes to the interim consolidated financial statements

Table of Contents**lululemon athletica inc. and Subsidiaries****CONSOLIDATED STATEMENTS OF OPERATIONS**

	Thirteen Weeks Ended July 31, 2011	Thirteen Weeks Ended August 1, 2010	Twenty-Six Weeks Ended July 31, 2011	Twenty-Six Weeks Ended August 1, 2010
	(Unaudited)			
	(Amounts in thousands, except per share amounts)			
Net revenue	\$ 212,323	\$ 152,208	\$ 399,103	\$ 290,505
Cost of goods sold	90,251	71,910	167,346	135,850
Gross profit	122,072	80,298	231,757	154,655
Selling, general and administrative expenses	62,589	46,055	120,587	87,938
Income from operations	59,483	34,243	111,170	66,717
Other income (expense), net	597	2,092	1,501	2,254
Income before provision for income taxes	60,080	36,335	112,671	68,971
Provision for income taxes	21,462	14,628	40,537	27,676
Net income	38,618	21,707	72,134	41,295
Net income (loss) attributable to non-controlling interest	239	(85)	383	(85)
Net income attributable to lululemon athletica inc.	\$ 38,379	\$ 21,792	\$ 71,751	\$ 41,380
Net basic earnings per share	\$ 0.27	\$ 0.15	\$ 0.50	\$ 0.29
Net diluted earnings per share	\$ 0.26	\$ 0.15	\$ 0.49	\$ 0.29
Basic weighted-average number of shares outstanding	143,163	141,640	142,961	141,416
Diluted weighted-average number of shares outstanding	145,228	143,500	145,108	143,384

See accompanying notes to the interim consolidated financial statements

Table of Contents**lululemon athletica inc. and Subsidiaries****CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY**

	Exchangeable Stock		Special Voting Stock		Common Stock		Additional Paid-in Capital (Unaudited)	Retained Earnings	Other Comprehensive Income	Total	Non- Control Interests
	Shares	Par Value	Shares	Par Value	Shares	Par Value	(Unaudited)				
December 31, 2010	35,636	\$	35,636	\$	106,756	\$ 534	\$ 179,870	\$ 189,656	\$ 20,329	\$ 390,389	\$ 3,900
Net income:								71,751		71,751	
Other comprehensive income								16,087		16,087	
Compensation expense										87,838	
Gain from sale of equity								5,066		5,066	
Compensation expense issued upon vesting of exchangeable								4,391		4,391	
Issuance of restricted stock	(1,111)		(1,111)		1,111	5	(5)				
Exercise of restricted stock					901	5	7,700			7,705	
Change in non-controlling interests											38
December 31, 2011	34,525	\$	34,525	\$	108,773	\$ 544	\$ 197,022	\$ 261,407	\$ 36,416	\$ 495,389	\$ 4,280

See accompanying notes to the interim consolidated financial statements

Table of Contents**lululemon athletica inc. and Subsidiaries****CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Twenty-Six Weeks Ended July 31, 2011	Twenty-Six Weeks Ended August 1, 2010
	(Unaudited)	
	(Amounts in thousands)	
Cash flows from operating activities		
Net income attributable to lululemon athletica inc.	\$ 71,751	\$ 41,380
Net income (loss) attributable to non-controlling interest	\$ 383	\$ (85)
Net income	\$ 72,134	\$ 41,295
Items not affecting cash		
Depreciation and amortization	13,561	11,990
Stock-based compensation	5,066	3,563
Deferred income taxes	(10,487)	12,475
Excess tax benefits from stock-based compensation	(4,391)	(3,800)
Gain on investment		(1,792)
Other, including net changes in other non-cash balances		
Prepaid expenses and other current assets	(10,246)	(1,973)
Inventories	(30,164)	(17,777)
Accounts payable	(2,085)	(4,721)
Accrued liabilities	4,646	545
Income taxes payable	(17,927)	(5,129)
Other non-cash balances	(578)	(124)
Net cash provided by operating activities	19,529	34,552
Cash flows from investing activities		
Purchase of property and equipment	(87,324)	(11,571)
Acquisition of franchises		(12,482)
Net cash used in investing activities	(87,324)	(24,053)
Cash flows from financing activities		
Proceeds from exercise of stock options	7,704	2,338
Excess tax benefits from stock-based compensation	4,391	3,800
Net cash provided by financing activities	12,095	6,138
Effect of exchange rate changes on cash	4,142	1,962

Edgar Filing: lululemon athletica inc. - Form 10-Q

Increase (decrease) in cash and cash equivalents	(51,558)		18,599
Cash and cash equivalents, beginning of period	\$ 316,286	\$	159,573
Cash and cash equivalents, end of period	\$ 264,728	\$	178,172

See accompanying notes to the interim consolidated financial statements

Table of Contents

lululemon athletica inc. and Subsidiaries

**NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS
(Amounts in thousands, except per share and store count information, unless otherwise indicated)**

NOTE 1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Nature of operations

lululemon athletica inc., a Delaware corporation (lululemon and, together with its subsidiaries unless the context otherwise requires, the Company) is engaged in the design, manufacture and distribution of healthy lifestyle inspired athletic apparel, which is sold through a chain of corporate-owned and operated retail stores, direct to consumer through e-commerce, through independent franchises and through a network of wholesale accounts. The Company s primary markets are Canada, the United States and Australia, where 45, 89 and 13 corporate-owned stores were in operation as at July 31, 2011, respectively. There were 147 and 133 corporate-owned stores in operation as of July 31, 2011 and January 30, 2011, respectively.

Basis of presentation

The unaudited interim consolidated financial statements as of July 31, 2011 and for the twenty-six weeks ended July 31, 2011 and August 1, 2010 are presented using the United States dollar and have been prepared by the Company under the rules and regulations of the Securities and Exchange Commission (SEC). In the opinion of management, the financial information is presented in accordance with United States generally accepted accounting principles (GAAP) for interim financial information and, accordingly, do not include all of the information and footnotes required by GAAP for complete financial statements. The financial information as of January 30, 2011 is derived from the Company s audited consolidated financial statements and notes for the fiscal year ended January 30, 2011, included in Item 8 in the fiscal 2010 Annual Report on Form 10-K filed with the SEC on March 17, 2011. These unaudited interim consolidated financial statements reflect all adjustments which are in the opinion of management necessary to a fair statement of the results for the interim periods presented. These unaudited interim consolidated financial statements should be read in conjunction with the Company s consolidated financial statements and related notes included in the Company s 2010 Annual Report on Form 10-K.

The Company s fiscal year ends on the Sunday closest to January 31 of the following year, typically resulting in a 52 week year, but occasionally giving rise to an additional week, resulting in a 53 week year. Fiscal 2011 will end on January 29, 2012.

The Company s business is affected by the pattern of seasonality common to most retail apparel businesses. The results for the periods presented are not necessarily indicative of future financial results.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Property and equipment

Property and equipment are recorded at cost less accumulated depreciation. Direct internal and external costs related to software used for internal purposes which are incurred during the application development stage or for upgrades that add functionality are capitalized. All other costs related to internal use software are expensed as incurred.

Buildings are amortized on a straight-line basis over the expected useful life of the asset. Leasehold improvements are amortized on a straight-line basis over the lesser of the length of the lease, without consideration of option renewal

Edgar Filing: lululemon athletica inc. - Form 10-Q

periods, and the estimated useful life of the assets, to a maximum of five years. All other property and equipment are amortized using the declining balance method as follows. Amortization commences when an asset is ready for its intended use.

Furniture and fixtures	20%
Computer hardware and software	30%
Equipment and vehicles	30%

Table of Contents

lululemon athletica inc. and Subsidiaries

NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Recent accounting pronouncements

In April 2010, the Financial Accounting Standards Board (FASB) amended Accounting Standards Codification (ASC) Topic 718 *Compensation* (ASC 718) to clarify that a share-based payment award with an exercise price denominated in the currency of a market in which a substantial portion of the entity's equity securities trades should not be considered to contain a market, performance or service condition. Therefore, an entity should not classify such an award as a liability if it otherwise qualifies for classification in equity. This guidance is effective for interim and annual periods beginning on or after December 15, 2010 and is to be applied prospectively. The Company adopted the amendment in the first quarter of fiscal 2011 with no material impact on the Company's consolidated financial statements.

In May 2011, the FASB amended ASC Topic 820 *Fair Value Measurement* (ASC 820) to clarify requirements for how to measure fair value and for disclosing information about fair value measurements common to US GAAP and International Financial Reporting Standards. This guidance is effective for interim and annual periods beginning on or after December 15, 2011. The Company will adopt the amendment in the first quarter of fiscal 2012 and expects no material impact on the Company's consolidated financial statements.

In June 2011, the FASB amended ASC 820 to require (i) that all non-owner changes in stockholders' equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements, and (ii) presentation of reclassification adjustments from other comprehensive income (OCI) to net income on the face of the financial statements. This guidance eliminates the option to present the components of OCI as part of the statement of changes in stockholders' equity, but does not change the items that must be reported in OCI or when an item of OCI must be reclassified to net income. This guidance is effective for years, and interim periods within those years, beginning after December 15, 2011. The Company will adopt the amendment in fiscal 2012 and expects no material impact on the Company's consolidated financial statements.

NOTE 3. STOCKHOLDER S EQUITY

On June 8, 2011 the Company's stockholders approved a two-for-one stock split (the Stock Split) of the Company's common stock and an increase in the Company's authorized common stock from 200,000 shares to 400,000 shares. Shares of the Company's common stock traded on a post-split basis on July 12, 2011 on the Nasdaq Stock Market and July 6, 2011 on the Toronto Stock Exchange. In connection with the Stock Split, the stockholders also approved a two-for-one split of the Company's exchangeable special voting stock and an increase in the Company's authorized exchangeable special voting stock from 30,000 to 60,000.

NOTE 4. STOCK-BASED COMPENSATION

Share option plans

The Company's employees participate in various stock-based compensation plans, which are either provided by a principal stockholder of the Company or by the Company directly.

Stock-based compensation expense charged to income for the plans was \$5,066 and \$3,563 for the twenty-six weeks ended July 31, 2011 and August 1, 2010, respectively. Total unrecognized compensation cost as at July 31, 2011 was \$22,323 for all stock award plans, which is expected to be recognized over a weighted-average period of 2.5 years.

Table of Contents**lululemon athletica inc. and Subsidiaries****NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)*****Company stock options and performance stock units***

A summary of the Company's stock option, performance stock unit and restricted share activity as of July 31, 2011 and changes during the twenty-six week period then ended is presented on a post-split basis below:

	Number of Stock Options	Weighted- Average Exercise Price	Number of Performance Units	Weighted- Average Grant Fair Value	Number of Restricted Shares	Weighted- Average Grant Fair Value
Balance at January 30, 2011	3,270	\$ 10.83	174	\$ 20.96	8	\$ 21.22
Granted	118	\$ 39.84	201	39.01	8	47.55
Exercised	901	\$ 8.55				
Forfeited	38	\$ 8.08				
Balance at July 31, 2011	2,449	\$ 13.11	375	\$ 30.63	16	\$ 34.17
Exercisable at July 31, 2011	488	\$ 6.20		\$		\$

The Company's performance stock units are awarded to eligible employees and entitle the grantee to receive up to 1.5 shares of common stock per performance stock unit if the Company achieves specified performance goals and the grantee remains employed during the vesting period. The fair value of performance stock units is based on the closing price of the Company's common stock on the award date. Expense for performance stock units is recognized when it is probable that the performance goal will be achieved.

Stockholder-sponsored stock options

During the thirteen weeks ended July 31, 2011, holders of exchangeable shares converted 491 exchangeable shares into 491 shares of common stock of the Company for no additional consideration. In connection with the exchange of exchangeable shares, an equal number of outstanding shares of the Company's special voting stock were cancelled.

During the thirteen weeks ended July 31, 2011, there were no grants or forfeitures related to the stock options issued and outstanding under the stockholder-sponsored awards.

Employee stock purchase plan

The Company's Employee Stock Purchase Plan (ESPP) allows for the purchase of common stock of the Company by all eligible employees. Eligible employees may elect to have whatever portion of his or her base salary equates, after deduction of applicable taxes, to either 3%, 6% or 9% of his or her base salary withheld during each payroll period for purposes of purchasing shares of the Company's common stock under the ESPP. Additionally, the Company or the subsidiary of the Company employing the participant, will make a cash contribution as additional compensation to

each participant equal to one-third of the aggregate amount of that participant's contribution for that pay period, which will be used to purchase shares of the Company's common stock, subject to certain limits as defined in the ESPP. The maximum number of shares available under the ESPP is 6,000 shares. During the thirteen weeks ended July 31, 2011, there were 15 shares purchased under the ESPP, which were funded by the Company through open market purchases.

Table of Contents**lululemon athletica inc. and Subsidiaries****NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 5. EARNINGS PER SHARE**

Following with the Stock Split, the Company retroactively adjusted EPS for the thirteen and twenty-six week periods ended July 31, 2011 and August 1, 2010 in accordance with ASC topic 260, *Earnings Per Share* (ASC 260). The details of the computation of basic and diluted earnings per share are as follows:

	Thirteen Weeks Ended July 31, 2011	Thirteen Weeks Ended August 1, 2010	Twenty-Six Weeks Ended July 31, 2011	Twenty-Six Weeks Ended August 1, 2010
Net income	\$ 38,618	\$ 21,707	\$ 72,134	\$ 41,295
Net income (loss) attributable to non-controlling interest	\$ 239	\$ (85)	\$ 383	\$ (85)
Net income attributable to lululemon athletica inc.	\$ 38,379	\$ 21,792	\$ 71,751	\$ 41,380
Basic weighted-average number of shares outstanding	143,163	141,640	142,961	141,416
Effect of stock options assume exercised	2,065	1,860	2,147	1,968
Diluted weighted-average number of shares outstanding	145,228	143,500	145,108	143,384
Net basic earnings per share	\$ 0.27	\$ 0.15	\$ 0.50	\$ 0.29
Net diluted earnings per share	\$ 0.26	\$ 0.15	\$ 0.49	\$ 0.29

The Company's calculation of weighted-average shares includes the common stock of the Company as well as the exchangeable shares. Weighted-average shares for the thirteen and twenty-six weeks ended August 1, 2010 have been calculated as if the Stock Split was in effect at February 1, 2010. Exchangeable shares are the equivalent of common shares in all material respects. All classes of stock have in effect the same rights and share equally in undistributed net income. For the twenty-six weeks ended July 31, 2011 and August 1, 2010, 31 and 128 stock options, respectively, were anti-dilutive to earnings and therefore have been excluded from the computation of diluted earnings per share.

Table of Contents**lululemon athletica inc. and Subsidiaries****NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 6. SUPPLEMENTARY FINANCIAL INFORMATION**

A summary of certain balance sheet accounts is as follows:

	July 31, 2011	January 30, 2011
Accounts receivable:		
Trade accounts receivable	\$ 3,628	\$ 2,596
Miscellaneous receivables	6,092	6,520
	\$ 9,720	\$ 9,116
Inventories:		
Finished goods	\$ 91,831	\$ 59,138
Raw materials	1,753	1,913
Provision to reduce inventory to market value	(4,700)	(3,582)
	\$ 88,884	\$ 57,469
Prepaid expenses and other current assets:		
Prepaid income tax installments	\$ 13,493	\$ 79
Other prepaid expenses and other current assets	7,147	6,329
	\$ 20,640	\$ 6,408
Property and equipment:		
Land	\$ 63,002	\$
Buildings	5,268	
Leasehold improvements	98,883	84,773
Furniture and fixtures	18,886	17,940
Computer hardware and software	44,296	34,581
Equipment and vehicles	1,312	1,038
Accumulated amortization and depreciation	(80,527)	(67,378)
	\$ 151,120	\$ 70,954
Goodwill and intangible assets:		
Goodwill	\$ 18,437	\$ 18,437
Changes in foreign currency exchange rates	3,562	1,837
	21,999	20,274
Reacquired franchise rights	10,709	10,709

Edgar Filing: lululemon athletica inc. - Form 10-Q

Non-competition agreements	694	694
Accumulated amortization	(7,328)	(6,355)
Changes in foreign currency exchange rates	2,360	1,790
	6,435	6,838
	\$ 28,434	\$ 27,112
Other non-current assets:		
Prepaid rent and security deposits	\$ 3,342	\$ 2,762
Deferred lease cost	1,214	1,301
	\$ 4,556	\$ 4,063
Accrued liabilities:		
Inventory purchases	\$ 12,562	\$ 11,925
Sales tax collected	5,088	4,505
Accrued rent	2,753	2,750
Lease exit costs	723	1,317
Other	7,683	4,769
	\$ 28,809	\$ 25,266
Non-current liabilities:		
Deferred lease liability	\$ 14,359	\$ 13,129
Tenant inducements	7,467	6,516
	\$ 21,826	\$ 19,645

Table of Contents**lululemon athletica inc. and Subsidiaries****NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 7. SEGMENT REPORTING**

The Company reports segments based on the financial information it uses in managing its business. The Company's reportable segments are comprised of corporate-owned stores, direct to consumer and other. Direct to consumer includes sales from the Company's e-commerce website and phone sales. Franchise sales, wholesale, showrooms sales and outlet sales have been combined into other. The Company has reviewed its general corporate expenses and determined some costs previously classified as general corporate are direct segment expenses. Accordingly, all prior year comparable information has been reclassified to conform to the current year classification. Information for these segments is detailed in the table below:

	Thirteen Weeks Ended July 31, 2011	Thirteen Weeks Ended August 1, 2010	Twenty-Six Weeks Ended July 31, 2011	Twenty-Six Weeks Ended August 1, 2010
Net revenue:				
Corporate-owned stores	\$ 178,198	\$ 129,443	\$ 334,719	\$ 245,017
Direct to consumer	18,579	9,634	32,371	18,776
Other	15,546	13,131	32,013	26,712
	\$ 212,323	\$ 152,208	\$ 399,103	\$ 290,505
Income from operations before general corporate expense:				
Corporate-owned stores	\$ 64,281	\$ 42,426	\$ 123,576	\$ 80,873
Direct to consumer	8,173	2,002	12,459	4,561
Other	4,702	3,126	9,686	7,156
	77,156	47,554	145,721	92,590
General corporate expense	17,673	13,311	34,551	25,874
Income from operations	59,483	34,243	111,170	66,717
Other income (expense), net	597	2,092	1,501	2,254
Income before provision for income taxes	\$ 60,080	\$ 36,355	\$ 112,671	\$ 68,971
Capital expenditures:				
Corporate-owned stores	\$ 7,229	\$ 1,875	\$ 12,378	\$ 4,117
Direct to consumer	2,120	2,452	3,136	2,452
Corporate	3,144	1,366	71,810	5,002
	\$ 12,493	\$ 5,693	\$ 87,324	\$ 11,571

Edgar Filing: lululemon athletica inc. - Form 10-Q

Depreciation:

Corporate-owned stores	\$	4,643	\$	3,758	\$	8,501	\$	7,529
Direct to consumer		630		46		892		94
Corporate		2,248		2,730		4,168		4,299
	\$	7,521	\$	6,534	\$	13,561	\$	11,922

Table of Contents

ITEM 2. *MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS*

Some of the statements contained in this Form 10-Q and any documents incorporated herein by reference constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical facts, included or incorporated in this Form 10-Q are forward-looking statements, particularly statements which relate to expectations, beliefs, projections, future plans and strategies, anticipated events or trends and similar expressions concerning matters that are not historical facts, such as statements regarding our future financial condition or results of operations, our prospects and strategies for future growth, the development and introduction of new products, and the implementation of our marketing and branding strategies. In many cases, you can identify forward-looking statements by terms such as may, will, should, expects, plans, anticipates, believes, estimates, intends, predicts, potential, or other comparable terminology.

The forward-looking statements contained in this Form 10-Q and any documents incorporated herein by reference reflect our current views about future events and are subject to risks, uncertainties, assumptions and changes in circumstances that may cause events or our actual activities or results to differ significantly from those expressed in any forward-looking statement. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future events, results, actions, levels of activity, performance or achievements. Readers are cautioned not to place undue reliance on these forward-looking statements. A number of important factors could cause actual results to differ materially from those indicated by the forward-looking statements, including, but not limited to, those factors described in **Risk Factors** and elsewhere in this report.

The forward-looking statements contained in this Form 10-Q reflect our views and assumptions only as of the date of this Form 10-Q and are expressly qualified in their entirety by the cautionary statements included in this Form 10-Q. Except as required by applicable securities law, we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events.

Our fiscal year ends on the Sunday closest to January 31 of the following year, typically resulting in a 52 week year, but occasionally gives rise to an additional week, resulting in a 53 week year. Fiscal 2011 will end on January 29, 2012.

Overview

Our results for the first two quarters of fiscal 2011 demonstrate the ongoing success of our efforts to execute our strategic plan. We remain committed to investing in our stores and our people, making infrastructure enhancements and funding working capital requirements, while remaining conscious of our discretionary spending. We continually assess the economic environment and market conditions when making decisions regarding our expansion investments. We believe our strong cash flow generation, solid balance sheet and healthy liquidity provide us with the financial flexibility to continue executing the initiatives which we believe will be beneficial for the Company.

We believe that our brand is recognized as premium in our offerings of yoga and run assortment, as well as a leader in technical fabrics and quality construction. This has made our product desirable to our consumers and has driven demand, and resulted in top-line growth. We experienced strong sell through of our merchandise which minimized markdowns and discounts, driving a strong gross margin in the first two quarters of fiscal 2011.

We saw continuing increases in traffic and conversion rates on our e-commerce website in fiscal 2010, which led us to believe that there is potential for our direct to consumer segment to become an increasingly substantial part of our

business. We committed a portion of our resources to further developing this channel, making infrastructure changes in the first half of fiscal 2011 which included bringing the operations in-house and updating the operating platform. Investments in the infrastructure will continue through the remainder of the fiscal year as we see our e-commerce website as an opportunity to increase our brand awareness in international markets.

Table of Contents

In the first half of fiscal 2011, we opened 12 new corporate-owned stores in North America and two new corporate-owned stores in Australia. In March 2011, we purchased the building that housed our administrative offices. We also invested in our people, which included wage increases to employees in our corporate-owned stores and other channels.

Operating Segment Overview

lululemon is a designer and retailer of technical athletic apparel operating primarily in North America and Australia. Our yoga-inspired apparel is marketed under the lululemon athletica and ivivva athletica brand names. We offer a comprehensive line of apparel and accessories including fitness pants, shorts, tops and jackets designed for athletic pursuits such as yoga, running and general fitness, and technical clothing for active female youth. As of July 31, 2011, our branded apparel was principally sold through 151 corporate-owned and franchise stores that are primarily located in Canada, the United States and Australia, and via our e-commerce website through our direct to consumer channel. We believe our vertical retail strategy allows us to interact more directly with and gain insights from our customers while providing us with greater control of our brand. For the second quarter of fiscal 2011, approximately 45% of our net revenue was derived from sales of our products in Canada, 51% of our net revenue was derived from the sales of our products in the United States, and the remaining 4% of our net revenue was derived from sales of our products outside of North America.

Our net revenue has grown from \$40.7 million in fiscal 2004 to \$711.7 million in fiscal 2010. This represents a compound annual growth rate of 61%. Our net revenue also increased from \$152.2 million in the second quarter of fiscal 2010 to \$212.3 million in the second quarter of fiscal 2011, representing a 39% increase. Our increase in net revenue from fiscal 2004 to fiscal 2010 resulted from comparable store sales growth as high as 37%, which we realized in fiscal 2010, and from the addition of retail locations, including:

12 net new corporate-owned stores in North America in fiscal 2010, which included one franchised store that was reacquired, and 11 net new corporate-owned stores in Australia, which included nine franchised stores that were reacquired;

seven net new corporate-owned stores in North America in fiscal 2009;

34 net new corporate-owned stores in North America in fiscal 2008; and

31 net new corporate-owned stores in North America in fiscal 2007.

Our ability to open new stores and grow sales in existing stores has been driven by increasing demand for our technical athletic apparel and a growing recognition of the lululemon athletica brand. We believe our superior products, strategic store locations, inviting store environment, and distinctive corporate culture are responsible for our strong financial performance.

We have three reportable segments: corporate-owned stores, direct to consumer and other. We report our segments based on the financial information we use in managing our businesses. While we receive financial information for each corporate-owned store, we have aggregated all of the corporate-owned stores into one reportable segment due to the similarities in the economic and other characteristics of these stores. Expanding our direct to consumer sales channel is a significant part of our near-term growth strategy, and we therefore expect the revenue derived from our direct to consumer sales to comprise more than 10% of the net revenue we report in future fiscal years. Our other operations, which include franchise sales, wholesale, showrooms sales and outlet sales, each accounted for less than 10% of our net revenues from continuing operations in each of the first and second quarter of fiscal 2011, and fiscal 2010.

Table of Contents**Results of Operations*****Thirteen Week Results***

The following table summarizes key components of our results of operations for the thirteen week periods ended July 31, 2011 and August 1, 2010. The operating results are expressed in dollar amounts as well as relevant percentages, presented as a percentage of net revenue.

	Thirteen Weeks Ended July 31, 2011 and August 1, 2010			
	2011	2010	2011	2010
	(In thousands)		(Percentages)	
Net revenue	\$ 212,323	\$ 152,208	100.0	100.0
Cost of goods sold	90,251	71,910	42.5	47.2
Gross profit	122,072	80,298	57.5	52.8
Selling, general and administrative expenses	62,589	46,055	29.5	30.3
Income from operations	59,483	34,243	28.0	22.5
Other income (expense), net	597	2,092	0.3	1.4
Income before provision for income taxes	60,080	36,335	28.3	23.9
Provision for income taxes	21,462	14,628	10.1	9.6
Net income	38,618	21,707	18.2	14.3
Net income (loss) attributable to non-controlling interest	239	(85)	0.1	(0.0)
Net income attributable to lululemon athletica inc.	\$ 38,379	\$ 21,792	18.1	14.3

Net Revenue

Net revenue increased \$60.1 million, or 39%, to \$212.3 million for the second quarter of fiscal 2011 from \$152.2 million for the second quarter of fiscal 2010. Assuming the average exchange rate between the Canadian and United States dollars and the Australian and United States dollars for the second quarter of fiscal 2010 remained constant, our net revenue would have increased \$51.8 million, or 34%, for the second quarter of fiscal 2011.

The net revenue increase was driven by increased sales at locations in our comparable stores base, sales from new stores opened and the growth of our e-commerce website sales included in our direct to consumer segment. The constant dollar increase in comparable store sales was driven primarily by the strength of our existing product lines, successful introduction of new products and increasing recognition of the lululemon athletica brand name, especially at our U.S. stores.

Our net revenue on a segment basis for the thirteen week periods ended July 31, 2011 and August 1, 2010 are expressed in dollar amounts as well as relevant percentages, presented as a percentage of total net revenue below.

**Thirteen Weeks Ended July 31, 2011 and
August 1, 2010**

	2011	2010	2011	2010
	(In thousands)		(Percentages)	

Corporate-owned stores	\$ 178,198	\$ 129,443	83.9	85.1
Direct to consumer	18,579	9,634	8.8	6.3
Other	15,546	13,131	7.3	8.6
Net revenue	\$ 212,323	\$ 152,208	100.0	100.0

Table of Contents

Corporate-Owned Stores. Net revenue from our corporate-owned stores segment increased \$48.8 million, or 38%, to \$178.2 million in the second quarter of fiscal 2011 from \$129.4 million in the second quarter of fiscal 2010. The following contributed to the increase in net revenue from our corporate-owned stores segment:

Comparable store sales increase of 25% in the second quarter of fiscal 2011 resulted in a \$29.8 million increase to net revenue, including the effect of foreign currency fluctuations. Excluding the effect of foreign currency fluctuations, comparable store sales increased 20%, or \$23.1 million, in the second quarter of fiscal 2011; and

Net revenue from corporate-owned stores we opened subsequent to August 1, 2010, and therefore not included in the comparable store sales growth, contributed \$19.0 million of the increase. Net new store openings since the second quarter of fiscal 2010 included 18 stores in the United States and three stores in Australia.

Direct to Consumer. Net revenue from our direct to consumer segment increased \$9.0 million, or 93%, to \$18.6 million in the second quarter of fiscal 2011 from \$9.6 million in the second quarter of fiscal 2010. The increase in net revenue was the result of increased traffic to our e-commerce website, as well as higher conversion rates and average order value.

Other. Net revenue from our other segment increased \$2.4 million, or 18%, to \$15.5 million in the second quarter of fiscal 2011 from \$13.1 million in the second quarter of fiscal 2010. This increase was a result of increased net revenues from strategic sales, showrooms and outlets, partially offset by decreased net revenues from our franchise operating channel. Our other segment continues to grow year over year through new showroom locations, new wholesale customers and net revenue growth at existing locations attributable to a strong product offering and brand interest. We continue to employ our other segment strategy to increase interest in our product in markets we have not otherwise entered with corporate-owned stores.

Gross Profit

Gross profit increased \$41.8 million, or 52%, to \$122.1 million for the second quarter of fiscal 2011 from \$80.3 million for the second quarter of fiscal 2010. Increased net revenues as well as a strengthening Canadian dollar relative to the U.S. dollar improved product margin in all of our operating segments, and ultimately resulted in an increased gross profit.

The increase in gross profit was partially offset by increases in fixed costs, such as occupancy costs and depreciation, as well as increased costs related to our design, merchandising, and production departments.

Gross profit as a percentage of net revenue, or gross margin, increased by 470 basis points, to 57.5% in the second quarter of fiscal 2011 from 52.8% in the second quarter of fiscal 2010. The increase in gross margin resulted primarily from:

an increase in product margins, which contributed to an increase in gross margin of 210 basis points, resulting from strong sell throughs of summer merchandise with fewer markdowns and discounts which was partially offset by product cost pressures from raw materials and labour costs.

a decrease in fixed costs, such as occupancy costs and depreciation, relative to the increase in net revenue, which had a leveraging effect on gross margin and contributed to an increase in gross margin of 120 basis points;

an improvement in the Canadian and Australian dollars, relative to the U.S. dollar, decreased foreign exchange impacts on product costs and contributed to an increase in gross margin of 100 basis points; and

a decrease in expenses related to our product and supply chain departments, relative to the increase in net revenue, which had a leveraging effect on gross margin and contributed to an increase in gross margin of 40 basis points.

Our cost of goods sold in the second quarter of fiscal 2011 and fiscal 2010 included \$0.4 million and \$0.4 million, respectively, of stock-based compensation.

Table of Contents

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased \$16.5 million, or 36%, to \$62.6 million in the second quarter of fiscal 2011 from \$46.1 million in the second quarter of fiscal 2010. The \$16.5 million increase in selling, general and administrative expenses was principally comprised of:

an increase in employee costs of \$10.5 million as we experience natural growth in labor hours associated with new and existing corporate-owned stores, showrooms, outlets and other, as well as an increase in wages as we invest in our employees;

an increase in other costs, including occupancy costs, depreciation and distribution not included in cost of goods sold, of \$5.1 million as a result of the expansion of our business; and

an increase in head office employee costs, including stock-based compensation expense and management incentive-based compensation, of \$2.3 million incurred in order to position us for long-term growth.

The increase in selling, general and administrative expenses was partially offset by a decrease in administrative costs related to our direct to consumer segment of \$1.4 million. This decrease was primarily associated with reduced professional fees resulting from bringing our e-commerce operations in-house.

As a percentage of net revenue, selling, general and administrative expenses decreased 80 basis points, to 29.5% in the second quarter of fiscal 2011 from 30.3% in the second quarter of fiscal 2010. The decrease in selling, general and administrative expenses as a percentage of net revenue was mainly due to the decreased administrative costs related to our direct to consumer segment.

Our selling, general and administrative expenses in the second quarter of fiscal 2011 and fiscal 2010 included \$1.9 million and \$1.5 million, respectively, of stock-based compensation expense.

Income from Operations

Income from operations increased \$25.2 million, or 74%, to \$59.5 million in the second quarter of fiscal 2011 from \$34.2 million in the second quarter of fiscal 2010. The increase was a result of increased gross profit of \$41.8 million, partially offset by increased selling, general and administrative costs of \$16.5 million. The increase in selling, general and administrative costs was primarily driven by the increase in our business, as seen in our net revenue increases.

On a segment basis, we determine income from operations without taking into account our general corporate expenses. We have reviewed our general corporate expenses and determined some costs previously classified as general corporate are direct segment expenses. Accordingly, all prior year comparable information has been reclassified to conform to the current year classification.

Income from operations (before general corporate expenses) for the thirteen weeks ended July 31, 2011 and August 1, 2010 are expressed in dollar amounts as well as percentages, presented as a percentage of net revenue of their respective operating segments below.

Thirteen Weeks Ended July 31, 2011 and August 1, 2010			
2011	2010	2011	2010
(In thousands)		(Percentages)	

Edgar Filing: lululemon athletica inc. - Form 10-Q

Corporate-owned stores	\$ 64,281	\$ 42,426	36.1	32.8
Direct to consumer	8,173	2,002	44.0	20.8
Other	4,702	3,126	30.2	23.8
Income from operations before general corporate expense	\$ 77,156	\$ 47,554		

Corporate-Owned Stores. Income from operations from our corporate-owned stores segment increased \$21.9 million, or 52%, to \$64.3 million for the second quarter of fiscal 2011 from \$42.4 million for the second quarter of fiscal 2010 primarily due to an increase of \$33.6 million in gross profit, which was offset partially by a

Table of Contents

natural increase in selling, general and administrative expenses related to employee costs as well as operating expenses associated with new stores and net revenue growth at existing stores.

Direct to Consumer. Income from operations from our direct to consumer segment increased \$6.2 million, or 310%, to \$8.2 million for the second quarter of fiscal 2011 from \$2.0 million for the second quarter of fiscal 2010. This increase was primarily the result of increased sales through our e-commerce website.

Other. Income from operations from our other segment increased \$1.6 million, or 52%, to \$4.7 million for the second quarter of fiscal 2011 from \$3.1 million for the second quarter of fiscal 2010. Gross profit related to our other segment increased \$2.1 million in the second quarter of fiscal 2011 from the second quarter of fiscal 2010. This increase was a result of increased income from strategic sales, showrooms and outlets, partially offset by decreased income from our franchise operating channel. Our other segment continues to grow year over year through new showroom locations, new wholesale customers and net revenue growth at existing locations attributable to a strong product offering and brand interest. We continue to employ our other segment strategy to increase interest in our product in markets we have not otherwise entered with corporate-owned stores.

Other Income (Expense), Net

Other income (expense), net decreased \$1.5 million, or 71%, to \$0.6 million in the second quarter of fiscal 2011 from \$2.1 million in the second quarter of fiscal 2010. The decrease was primarily a result of a gain being recorded in fiscal 2010 as a result of re-measuring our 13 percent non-controlling equity investment in Australia immediately before obtaining control of the same business.

Provision for Income Taxes

Provision for income taxes increased \$6.8 million, or 46.7%, to \$21.5 million in the second quarter of fiscal 2011 from \$14.6 million in the second quarter of fiscal 2010. In the second quarter of fiscal 2011, our effective tax rate was 35.7% compared to 40.3% in the second quarter of fiscal 2010. The decrease resulted from a revision to management's plans for repatriation of unremitted earnings of the Canadian operating subsidiary.

Net Income

Net income increased \$16.6 million to \$38.4 million for the second quarter of fiscal 2011 from \$21.8 million for the second quarter of fiscal 2010. The increase in net income of \$16.6 million for the second quarter of fiscal 2011 was a result of an increase in gross profit of \$41.8 million resulting from increased product sales and improved foreign exchange differences, offset by an increase in selling, general and administrative expenses of \$16.5 million, an increase in provision for income taxes of \$6.8 million, and a decrease in Other Income (Expense), Net of \$1.5 million.

Table of Contents**Twenty-Six Week Results**

The following table summarizes key components of our results of operations for the twenty-six week periods ended July 31, 2011 and August 1, 2010. The operating results are expressed in dollar amounts as well as relevant percentages, presented as a percentage of net revenue.

	Twenty-Six Weeks Ended July 31, 2011 and August 1, 2010			
	2011	2010	2011	2010
	(In thousands)		(Percentages)	
Net revenue	\$ 399,103	\$ 290,505	100.0	100.0
Cost of goods sold	167,346	135,850	41.9	46.8
Gross profit	231,757	154,655	58.1	53.2
Selling, general and administrative expenses	120,587	87,938	30.2	30.3
Income from operations	111,170	66,717	27.9	22.9
Other income (expense), net	1,501	2,254	0.4	0.8
Income before provision for income taxes	112,671	68,971	28.3	23.7
Provision for income taxes	40,537	27,676	10.2	9.5
Net income	72,134	41,295	18.1	14.2
Net income (loss) attributable to non-controlling interest	383	(85)	0.1	0.0
Net income attributable to lululemon athletica inc	\$ 71,751	\$ 41,380	18.0	14.2

Net Revenue

Net revenue increased \$108.6 million, or 37%, to \$399.1 million for the first two quarters of fiscal 2011 from \$290.5 million for the first two quarters of fiscal 2010. Assuming the average exchange rate between the Canadian and United States dollars and the Australian and United States dollars for the first two quarters of fiscal 2010 remained constant, our net revenue would have increased \$95.9 million, or 33%, for the first two quarters of fiscal 2011.

The net revenue increase was driven by increased sales at locations in our comparable stores base, sales from new stores opened, sales from franchised stores that were reacquired during the second quarter of fiscal 2010 and the growth of our e-commerce website sales included in our direct to consumer segment. The constant dollar increase in comparable store sales was driven primarily by the strength of our existing product lines, our successful introduction of new products and increasing recognition of the lululemon athletica brand name, especially at our U.S. stores.

Our net revenue on a segment basis for the twenty-six week periods ended July 31, 2011 and August 1, 2010 are expressed in dollar amounts as well as relevant percentages, presented as a percentage of total net revenue below.

Twenty-Six Weeks Ended July 31, 2011 and

	August 1, 2010			
	2011	2010	2011	2010
	(In thousands)		(Percentages)	
Corporate-owned stores	\$ 334,719	\$ 245,017	83.9	84.3
Direct to consumer	32,371	18,776	8.1	6.5
Other	32,013	26,712	8.0	9.2
Net revenue	\$ 399,103	\$ 290,505	100.0	100.0

Corporate-Owned Stores. Net revenue from our corporate-owned stores segment increased \$89.7 million, or 37%, to \$334.7 million in the first two quarters of fiscal 2011 from \$245.0 million in the first two quarters of fiscal

Table of Contents

2010. The following contributed to the \$89.7 million increase in net revenue from our corporate-owned stores segment:

Comparable store sales increase of 23% in the first two quarters of fiscal 2011 resulted in a \$51.5 million increase to net revenue, including the effect of foreign currency fluctuations. Excluding the effect of foreign currency fluctuations, comparable store sales increased 18%, or \$41.1 million, in the first two quarters of fiscal 2011; and

Net revenue from corporate-owned stores we opened subsequent to August 1, 2010, and therefore not included in the comparable store sales growth, contributed \$38.2 million of the increase. Net new store openings since the first two quarters of fiscal 2010 included 18 stores in the United States and three stores in Australia.

Direct to consumer. Net revenue from our direct to consumer segment increased \$13.6 million, or 72%, to \$32.4 million in the first two quarters of fiscal 2011 from \$18.8 million in the first two quarters of fiscal 2010. The increase in net revenue was primarily the result of increased traffic at our e-commerce website.

Other. Net revenue from our other segment increased \$5.3 million, or 20%, to \$32.0 million in the first two quarters of fiscal 2011 from \$26.7 million in the first two quarters of fiscal 2010. This increase was a result of increased net revenues from strategic sales, showrooms and outlets, partially offset by decreased net revenues from our franchise operating channel. Our other segment continues to grow year over year through new showroom locations, new wholesale customers and net revenue growth at existing locations attributable to a strong product offering and brand interest. We continue to employ our other segment strategy to increase interest in our product in markets we have not otherwise entered with corporate-owned stores.

Gross Profit

Gross profit increased \$77.1 million, or 50%, to \$231.8 million for the first two quarters of fiscal 2011 from \$154.7 million for the first two quarters of fiscal 2010. Increased net revenues as well as a strengthening Canadian dollar relative to the U.S. dollar improved product margin in all of our operating segments, and ultimately resulted in an increased gross profit.

The increase in gross profit was partially offset by increases in fixed costs, such as occupancy costs and depreciation, as well as increased costs related to our production, design, distribution and merchandising departments.

Gross profit as a percentage of net revenue, or gross margin, increased by 490 basis points, to 58.1% in the first two quarters of fiscal 2011 from 53.2% in the first two quarters of fiscal 2010. The increase in gross margin resulted primarily from:

an increase in product margins, which contributed to an increase in gross margin of 160 basis points, resulting from strong sell throughs of summer merchandise with fewer markdowns and discounts which was partially offset by product cost pressures from raw materials and labour costs.

a decrease in product costs related to a non-recurring adjustment for the recognition of input tax credits from previous periods of 70 basis points;

a decrease in fixed costs, such as occupancy costs and depreciation, relative to the increase in net revenue, which had a leveraging effect on gross margin and contributed to an increase in gross margin of 120 basis points;

an improvement in the Canadian and Australian dollars, relative to the U.S. dollar, decreased foreign exchange impacts on product costs and contributed to an increase in gross margin of 90 basis points; and

a decrease in expenses related to our product and supply chain departments, relative to the increase in net revenue, which had a leveraging effect on gross margin and contributed to an increase in gross margin of 50 basis points.

Table of Contents

Our cost of goods sold in the first two quarters of fiscal 2011 and fiscal 2010 included \$1.2 million and \$0.7 million, respectively, of stock-based compensation.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased \$32.6 million, or 37%, to \$120.6 million in the first two quarters of fiscal 2011 from \$87.9 million in the first two quarters of fiscal 2010. The \$32.6 million increase in selling, general and administrative expenses was principally comprised of:

an increase in employee costs of \$13.3 million as we experience natural growth in labor hours associated with new and existing corporate-owned stores, showrooms, outlets and other, as well as an increase in wages as we invest in our employees;

an increase in other costs, including occupancy costs, depreciation and distribution not included in cost of goods sold, of \$9.5 million as a result of the expansion of our business;

an increase in head office employee costs, including options expense and management incentive-based compensation, of \$7.1 million incurred in order to position us for long-term growth;

an increase in administrative costs of \$3.2 million related to our Australian business, which we now report on a consolidated basis, but previously accounted for on an equity basis; and

The increase in selling, general and administrative expenses was partially offset by a \$0.5 million decrease in administrative expenses related to our direct to consumer segment. This decrease was primarily associated of reduced professional fees resulting from bringing our e-commerce operations in-house, offset by costs associated with our infrastructure changes.

As a percentage of net revenue, selling, general and administrative expenses decreased 10 basis points, to 30.2% in the second quarter of fiscal 2011 from 30.3% in the second quarter of fiscal 2010.

Our selling, general and administrative expenses in the first two quarters of fiscal 2011 and fiscal 2010 included \$3.9 million and \$2.8 million, respectively, of stock-based compensation expense.

Income from Operations

Income from operations increased \$44.5 million, or 67%, to \$111.2 million in the first two quarters of fiscal 2011 from \$66.7 million in the first two quarters of fiscal 2010. The increase was a result of increased gross profit of \$77.1 million, partially offset by increased selling, general and administrative costs of \$32.6 million. The increase in selling, general and administrative costs was primarily driven by the increase in our business, as seen in our net revenue increases.

On a segment basis, we determine income from operations without taking into account our general corporate expenses. We have reviewed our general corporate expenses and determined some costs previously classified as general corporate are direct segment expenses. Accordingly, all prior year comparable information has been reclassified to conform to the current year classification.

Income from operations (before general corporate expenses) for the twenty-six week periods ended July 31, 2011 and August 1, 2010 are expressed in dollar amounts as well as percentages, presented as a percentage of net revenue of

their respective operating segments below.

	Twenty-Six Weeks Ended July 31, 2011 and August 1, 2010			
	2011	2010	2011	2010
	(In thousands)		(Percentages)	
Corporate-owned stores	\$ 123,576	\$ 80,873	36.9	33.0
Direct to consumer	12,459	4,561	38.5	24.3
Other	9,686	7,156	30.3	26.8
Income from operations before general corporate expense	\$ 145,721	\$ 92,590		

Table of Contents

Corporate-Owned Stores. Net income from our corporate-owned stores segment increased \$42.7 million, or 53%, to \$123.6 million for the first two quarters of fiscal 2011 from \$80.9 million for the first two quarters of fiscal 2010 primarily due to an increase of \$63.1 million in gross profit, which was offset partially by a natural increase in selling, general and administrative expenses related to employee costs as well as operating expenses associated with new stores and net revenue growth at existing stores.

Direct to consumer. Net income from our direct to consumer segment increased \$7.8 million, or 170%, to \$12.4 million for the first two quarters of fiscal 2011 from \$4.6 million for the first two quarters of fiscal 2010. The increase in net revenue was primarily the result of increased traffic at our e-commerce website.

Other. Net income from our other segment increased \$2.5 million, or 35%, to \$9.7 million for the first two quarters of fiscal 2011 from \$7.2 million for the first two quarters of fiscal 2010. This increase was a result of increased income from strategic sales, showrooms and outlets, partially offset by decreased income from our franchise operating channel. Our other segment continues to grow year over year through new showroom locations, new wholesale customers and net revenue growth at existing locations attributable to a strong product offering and brand interest. We continue to employ our other segment strategy to increase interest in our product in markets we have not otherwise entered with corporate-owned stores.

Other Income (Expense), Net

Other income (expense), net decreased \$0.8 million, or 33%, to \$1.5 million in the first two quarters of fiscal 2011 from \$2.3 million in the first two quarters of fiscal 2010. The decrease was primarily a result of a gain being recorded in fiscal 2010 as a result of re-measuring our 13 percent non-controlling equity investment in Australia immediately before obtaining control of the same business.

Provision for Income Taxes

Provision for income taxes increased \$12.9 million, or 47%, to \$40.5 million in the first two quarters of fiscal 2011 from \$27.7 million in the first two quarters of fiscal 2010. In the first two quarters of fiscal 2011, our effective tax rate was 36.0% compared to 40.1% in the first two quarters of fiscal 2010. The decrease resulted from a revision to managements plans for repatriation of unremitted earnings of the Canadian operating subsidiary.

Net Income

Net income increased \$30.4 million to \$71.8 million for the first two quarters of fiscal 2011 from \$41.4 million for the first two quarters of fiscal 2010. The increase in net income of \$71.8 million for the first two quarters of fiscal 2011 was a result of an increase in gross profit of \$77.1 million resulting from increased sales and improved foreign exchange differences, offset by an increase in selling, general and administrative expenses of \$32.6 million, an increase of \$12.9 million in provision for income taxes, and a decrease in other income (expense), net of \$0.8 million.

Seasonality

Historically, we have recognized a significant portion of our income from operations in the fourth fiscal quarter of each year as a result of increased sales during the holiday selling season. Despite the fact that we have experienced a significant amount of our net revenue and gross profit in the fourth quarter of each fiscal year, we believe that the true extent of the seasonality or cyclical nature of our business may have been overshadowed by our rapid growth to date.

Liquidity and Capital Resources

Our primary sources of liquidity are our current balances of cash and cash equivalents, cash flows from operations and borrowings available under our revolving credit facility. Our primary cash needs are capital expenditures for opening new stores and remodeling existing stores, making information technology system enhancements and funding working capital requirements. Cash and cash equivalents in excess of our needs are held in interest bearing accounts with financial institutions.

Table of Contents

At July 31, 2011, our working capital (excluding cash and cash equivalents) was a deficit of \$54.2 million and our cash and cash equivalents were \$264.7 million.

The following table summarizes our net cash flows provided by and used in operating, investing and financing activities for the periods indicated:

	Twenty-Six Weeks Ended July 31, 2011	Twenty-Six Weeks Ended August 1, 2010
	(In thousands)	
Total cash provided by (used in):		
Operating activities	\$ 19,529	\$ 34,552
Investing activities	(87,324)	(24,053)
Financing activities	12,095	6,138
Effect of exchange rate changes	4,142	1,962
Increase (decrease) in cash and cash equivalents	\$ (51,558)	\$ 18,599

Operating Activities

Operating Activities consist primarily of net income adjusted for certain non-cash items, including depreciation and amortization, deferred income taxes, stock-based compensation expense and the effect of the changes in non-cash working capital items, principally accounts receivable, inventories, accounts payable and accrued expenses.

Cash provided by operating activities decreased \$15.1 million, to \$19.5 million for the first two quarters of fiscal 2011 compared to \$34.6 million for the first two quarters of fiscal 2010. The \$15.1 million decrease was primarily a result of increased inventory purchases and higher income taxes paid in the first two quarters of fiscal 2011 compared to fiscal 2010.

Investing Activities

Investing Activities relate entirely to capital expenditures, advances to and investments in franchises and reacquisition of franchises.

Cash used in investing activities increased \$63.2 million, to \$87.3 million for the first two quarters of fiscal 2011 from \$24.1 million for the first two quarters of fiscal 2010. The \$63.2 million increase was primarily the result of the purchase of our principal executive and administrative offices for \$65.1 million plus acquisition-related costs. In the first two quarters of fiscal 2011 we opened 14 new corporate-owned stores compared to six new corporate-owned stores we opened in the first two quarters of fiscal 2010.

Financing Activities

Financing Activities consist primarily of cash received on the exercise of stock options and excess tax benefits from stock-based compensation. Cash provided by financing activities increased to \$12.1 million for the first two quarters of fiscal 2011 from \$6.1 million for the first two quarters of fiscal 2010.

We believe that our cash from operations and borrowings available to us under our revolving credit facility will be adequate to meet our liquidity needs and capital expenditure requirements for at least the next 24 months. Our cash from operations may be negatively impacted by a decrease in demand for our products as well as the other factors described in Risk Factors and elsewhere in this report. In addition, we may make discretionary capital improvements with respect to our stores, distribution facility, headquarters, or other systems, which we would expect to fund through the issuance of debt or equity securities or other external financing sources to the extent we were unable to fund such capital expenditures out of our cash from operations.

Table of Contents

Revolving Credit Facility

In April 2007, we executed a credit facility with the Royal Bank of Canada that provided for a CDN\$20.0 million uncommitted demand revolving credit facility to fund our working capital requirements. This agreement canceled our previous CDN\$8.0 million credit facility. Borrowings under this uncommitted credit facility are made on a when-and-as-needed basis at our discretion.

Borrowings under the credit facility can be made either as i) *Revolving Loans* Revolving loan borrowings will bear interest at a rate equal to the bank's CA\$ or US\$ annual base rate (defined as zero% plus the lender's annual prime rate) per annum, ii) *Offshore Loans* Offshore rate loan borrowings will bear interest at a rate equal to a base rate based upon LIBOR for the applicable interest period, plus 1.125% per annum, iii) *Bankers Acceptances* Bankers acceptance borrowings will bear interest at the bankers acceptance rate plus 1.125% per annum, or iv) *Letters of Credit and Letters of Guarantee* Borrowings drawn down under letters of credit or guarantee issued by the banks will bear a 1.125% per annum fee.

At July 31, 2011, aside from letters of credit and guarantees, there were no borrowings outstanding under this credit facility.

Off-Balance Sheet Arrangements

We enter into documentary letters of credit to facilitate the international purchase of merchandise. We also enter into standby letters of credit to secure certain of our obligations, including insurance programs and duties related to import purchases. As of July 31, 2011, letters of credit and letters of guarantee totaling \$1.5 million have been issued.

Other than these standby letters of credit and guarantee, we do not have any off-balance sheet arrangements, investments in special purpose entities or undisclosed borrowings or debt. In addition, we have not entered into any derivative contracts or synthetic leases.

Critical Accounting Policies

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions. Predicting future events is inherently an imprecise activity and, as such, requires the use of judgment. Actual results may vary from estimates in amounts that may be material to the financial statements. An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, and if different estimates that reasonably could have been used, or changes in the accounting estimates that are reasonably likely to occur periodically, could materially impact our consolidated financial statements. Our critical accounting policies and estimates are discussed in our Annual Report on Form 10-K for our 2010 fiscal year end filed with the SEC on March 17, 2011 and in Note 2 included in Item 1 of Part I of this Quarterly Report on Form 10-Q.

Table of Contents**Operating Locations**

Our operating locations by Canadian province, U.S. state and internationally as of July 31, 2011, and the overall totals as of July 31, 2011 and January 30, 2011, are summarized in the table below. While most of our stores are branded lululemon athletica, 3 of our corporate-owned stores are branded ivivva athletica and specialize in dance-inspired apparel for female youth.

	Corporate-Owned Stores	Franchise Stores	Total Stores
Canada			
Alberta	10		10
British Columbia	11		11
Manitoba	1		1
Nova Scotia	1		1
Ontario	17		17
Québec	4		4
Saskatchewan	1		1
Total Canada	45		45
United States			
Alabama	1		1
Arizona	2		2
California	20	1	21
Colorado		3	3
Connecticut	2		2
District of Columbia	2		2
Florida	6		6
Georgia	1		1
Hawaii	1		1
Illinois	8		8
Indiana	1		1
Maryland	2		2
Massachusetts	5		5
Michigan	1		1
Minnesota	2		2
Missouri	1		1
Nevada	1		1
New Jersey	3		3
New York	7		7
North Carolina	1		1
Ohio	2		2
Oregon	2		2
Pennsylvania	3		3
Tennessee	1		1
Texas	8		8
Virginia	3		3

Washington	3		3
Total United States	89	4	93
International			
Australia	13		13
Total International	13		13
Overall total, as of July 31, 2011	147	4	151
Overall total, as of January 30, 2011	133	4	137

Table of Contents

ITEM 3. *QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK*

Market risk represents the risk of loss that may impact our financial position due to adverse changes in financial market prices and rates. Our market risk exposure is primarily a result of fluctuations in interest rates and foreign currency exchange rates. We do not hold or issue financial instruments for trading purposes.

Foreign Currency Exchange Risk. We currently generate a significant portion of our net revenue in Canada. The reporting currency for our consolidated financial statements is the U.S. dollar. Historically, our operations were based largely in Canada. As of July 31, 2011, we operated 45 stores in Canada. As a result, we have been impacted by changes in exchange rates and may be impacted materially for the foreseeable future. As we recognize net revenue from sales in Canada in Canadian dollars, and the U.S. dollar has weakened during the first two quarters of fiscal 2011, it has had a positive impact on our Canadian operating results upon translation of those results into U.S. dollars for the purposes of consolidation. However, the gain in net revenue was partially offset by higher cost of sales and higher selling, general and administrative expenses that are generated in Canadian dollars. A 10% depreciation in the relative value of the Canadian dollar compared to the U.S. dollar would have resulted in lost income from operations of approximately \$5.7 million in the first two quarters of fiscal 2011. To the extent the ratio between our net revenue generated in Canadian dollars increases as compared to our expenses generated in Canadian dollars, we expect that our results of operations will be further impacted by changes in exchange rates. Additionally, a portion of our net revenue is generated in Australia. A 10% depreciation in the relative value of the Australian dollar compared to the U.S. dollar would have resulted in lost income from operations of approximately \$0.2 million in the first two quarters of fiscal 2011. We do not currently hedge foreign currency fluctuations. However, in the future, in an effort to mitigate losses associated with these risks, we may at times enter into derivative financial instruments, although we have not historically done so. We do not, and do not intend to, engage in the practice of trading derivative securities for profit.

Interest Rate Risk. In April 2007, we entered into an uncommitted senior secured demand revolving credit facility with Royal Bank of Canada. The revolving credit facility provides us with available borrowings in an amount up to CDN\$20.0 million. Because our revolving credit facility bears interest at a variable rate, we will be exposed to market risks relating to changes in interest rates, if we have a meaningful outstanding balance. As of July 31, 2011, we had no outstanding borrowings under our revolving facility. We currently do not engage in any interest rate hedging activity and currently have no intention to do so in the foreseeable future. However, in the future, if we have a meaningful outstanding balance under our revolving facility, in an effort to mitigate losses associated with these risks, we may at times enter into derivative financial instruments, although we have not historically done so. These may take the form of forward sales contracts, option contracts, and interest rate swaps. We do not, and do not intend to, engage in the practice of trading derivative securities for profit.

Inflation

Inflationary factors such as increases in the cost of our product and overhead costs may adversely affect our operating results. Although we do not believe that inflation has had a material impact on our financial position or results of operations to date, a high rate of inflation in the future may have an adverse effect on our ability to maintain current levels of gross margin and selling, general and administrative expenses as a percentage of net revenue if the selling prices of our products do not increase with these increased costs.

ITEM 4. *CONTROLS AND PROCEDURES*

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed by us in the reports we file or submit under the Securities Exchange Act of 1934, or 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 Chief Executive Officer (principal executive officer) and Chief Financial Officer (principal financial officer), to allow timely decisions to be made regarding required disclosure. We have established a Disclosure Committee, consisting of certain members of management, to assist in this evaluation. The Disclosure Committee meets on a quarterly basis, and as needed.

Our management, including our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated under

Table of Contents

the Exchange Act), at July 31, 2011. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, at July 31, 2011, our disclosure controls and procedures were effective.

There was no change in internal control over financial reporting during the fiscal thirteen weeks ended July 31, 2011 that has materially affected or is reasonably likely to materially affect our internal control over financial reporting.

PART II

OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are a party to various legal proceedings arising in the ordinary course of our business, but we are not currently a party to any legal proceeding that management believes would have a material adverse effect on our consolidated financial position or results of operations.

ITEM 1A. RISK FACTORS

In addition to the other information contained in this Form 10-Q and in our Annual Report on Form 10-K for our 2010 fiscal year, the following risk factors should be considered carefully in evaluating our business. Our business, financial condition or results of operations could be materially adversely affected by any of these risks. Please note that additional risks not presently known to us or that we currently deem immaterial could also impair our business and operations.

An economic downturn or economic uncertainty in our key markets may adversely affect consumer discretionary spending and demand for our products.

Many of our products may be considered discretionary items for consumers. Factors affecting the level of consumer spending for such discretionary items include general economic conditions, particularly those in Canada and the United States, and other factors such as consumer confidence in future economic conditions, fears of recession, the availability of consumer credit, levels of unemployment, tax rates and the cost of consumer credit. As global economic conditions continue to be volatile or economic uncertainty remains, trends in consumer discretionary spending also remain unpredictable and subject to reductions due to credit constraints and uncertainties about the future. The current volatility in the United States economy in particular has resulted in an overall slowing in growth in the retail sector because of decreased consumer spending, which may remain depressed for the foreseeable future. These unfavorable economic conditions may lead consumers to delay or reduce purchase of our products. Consumer demand for our products may not reach our sales targets, or may decline, when there is an economic downturn or economic uncertainty in our key markets, particularly in North America. Our sensitivity to economic cycles and any related fluctuation in consumer demand may have a material adverse effect on our financial condition.

Our sales and profitability may decline as a result of increasing product costs and decreasing selling prices.

Our business is subject to significant pressure on pricing and costs caused by many factors, including intense competition, constrained sourcing capacity and related inflationary pressure, pressure from consumers to reduce the prices we charge for our products and changes in consumer demand. These factors may cause us to experience increased costs, reduce our sales prices to consumers or experience reduced sales in response to increased prices, any of which could cause our operating margin to decline if we are unable to offset these factors with reductions in operating costs and could have a material adverse effect on our financial conditions.

Table of Contents

If we are unable to anticipate consumer preferences and successfully develop and introduce new, innovative and updated products, we may not be able to maintain or increase our sales and profitability.

Our success depends on our ability to identify and originate product trends as well as to anticipate and react to changing consumer demands in a timely manner. All of our products are subject to changing consumer preferences that cannot be predicted with certainty. If we are unable to introduce new products or novel technologies in a timely manner or our new products or technologies are not accepted by our customers, our competitors may introduce similar products in a more timely fashion, which could hurt our goal to be viewed as a leader in technical athletic apparel innovation. Our new products may not receive consumer acceptance as consumer preferences could shift rapidly to different types of athletic apparel or away from these types of products altogether, and our future success depends in part on our ability to anticipate and respond to these changes. Failure to anticipate and respond in a timely manner to changing consumer preferences could lead to, among other things, lower sales and excess inventory levels. Even if we are successful in anticipating consumer preferences, our ability to adequately react to and address those preferences will in part depend upon our continued ability to develop and introduce innovative, high-quality products. Our failure to effectively introduce new products that are accepted by consumers could result in a decrease in net revenues and excess inventory levels, which could have a material adverse effect on our financial condition.

Our results of operations could be materially harmed if we are unable to accurately forecast customer demand for our products.

To ensure adequate inventory supply, we must forecast inventory needs and place orders with our manufacturers based on our estimates of future demand for particular products. Our ability to accurately forecast demand for our products could be affected by many factors, including an increase or decrease in customer demand for our products or for products of our competitors, our failure to accurately forecast customer acceptance of new products, product introductions by competitors, unanticipated changes in general market conditions, and weakening of economic conditions or consumer confidence in future economic conditions. If we fail to accurately forecast customer demand we may experience excess inventory levels or a shortage of products available for sale in our stores or for delivery to customers.

Inventory levels in excess of customer demand may result in inventory write-downs or write-offs and the sale of excess inventory at discounted prices, which would cause our gross margin to suffer and could impair the strength and exclusivity of our brand. Conversely, if we underestimate customer demand for our products, our manufacturers may not be able to deliver products to meet our requirements, and this could result in damage to our reputation and customer relationships.

If we continue to grow at a rapid pace, we may not be able to effectively manage our growth and the increased complexity of our business and as a result our brand image and financial performance may suffer.

We have expanded our operations rapidly since our inception in 1998 and our net revenues have increased from \$40.7 million in fiscal 2004 to \$711.7 million in fiscal 2010. If our operations continue to grow at a rapid pace, we may experience difficulties in obtaining sufficient raw materials and manufacturing capacity to produce our products, as well as delays in production and shipments, as our products are subject to risks associated with overseas sourcing and manufacturing. We could be required to continue to expand our sales and marketing, product development and distribution functions, to upgrade our management information systems and other processes and technology, and to obtain more space for our expanding workforce. This expansion could increase the strain on our resources, and we could experience serious operating difficulties, including difficulties in hiring, training and managing an increasing number of employees. These difficulties could result in the erosion of our brand image which could have a material adverse effect on our financial condition.

Table of Contents

The fluctuating cost of raw materials could increase our cost of goods sold and cause our results of operations and financial condition to suffer.

The fabrics used by our suppliers and manufacturers include synthetic fabrics whose raw materials include petroleum-based products. Our products also include natural fibers, including cotton. Our costs for raw materials are affected by, among other things, weather, consumer demand, speculation on the commodities market, the relative valuations and fluctuations of the currencies of producer versus consumer countries and other factors that are generally unpredictable and beyond our control. Increases in the cost of raw materials, including petroleum or the prices we pay for our cotton yarn and cotton-based textiles, could have a material adverse effect on our cost of goods sold, results of operations, financial condition and cash flows.

We rely on third-party suppliers to provide fabrics for and to produce our products, and we have limited control over them and may not be able to obtain quality products on a timely basis or in sufficient quantity.

We do not manufacture our products or the raw materials for them and rely instead on third-party suppliers. Many of the specialty fabrics used in our products are technically advanced textile products developed and manufactured by third parties and may be available, in the short-term, from only one or a very limited number of sources. For example, Luon fabric, which is included in many of our products, is supplied to the mills we use by a single manufacturer in Taiwan, and the fibers used in manufacturing Luon fabric are supplied to our Taiwanese manufacturer by a single company. In fiscal 2010, approximately 69% of our products were produced by our top five manufacturing suppliers. We have no long term contracts with our suppliers or manufacturing sources, and we compete with other companies for fabrics, raw materials, production and import quota capacity.

We may experience a significant disruption in the supply of fabrics or raw materials from current sources or, in the event of a disruption, we may be unable to locate alternative materials suppliers of comparable quality at an acceptable price, or at all. In addition, if we experience significant increased demand, or if we need to replace an existing supplier manufacturer, we may be unable to locate additional supplies of fabrics or raw materials or additional manufacturing capacity on terms that are acceptable to us, or at all, or we may be unable to locate any supplier or manufacturer with sufficient capacity to meet our requirements or to fill our orders in a timely manner. Identifying a suitable supplier is an involved process that requires us to become satisfied with their quality control, responsiveness and service, financial stability and labor and other ethical practices. Even if we are able to expand existing or find new manufacturing or fabric sources, we may encounter delays in production and added costs as a result of the time it takes to train our suppliers and manufacturers in our methods, products and quality control standards. Delays related to supplier changes could also arise due to an increase in shipping times if new suppliers are located farther away from our markets or from other participants in our supply chain. Any delays, interruption or increased costs in the supply of fabric or manufacture of our products could have an adverse effect on our ability to meet customer demand for our products and our financial condition.

We operate in a highly competitive market and the size and resources of some of our competitors may allow them to compete more effectively than we can, resulting in a loss of our market share and a decrease in our net revenue and profitability.

The market for technical athletic apparel is highly competitive. Competition may result in pricing pressures, reduced profit margins or lost market share or a failure to grow our market share, any of which could substantially harm our business and results of operations. We compete directly against wholesalers and direct retailers of athletic apparel, including large, diversified apparel companies with substantial market share and established companies expanding their production and marketing of technical athletic apparel, as well as against retailers specifically focused on women's athletic apparel. We also face competition from wholesalers and direct retailers of traditional commodity athletic apparel, such as cotton T-shirts and sweatshirts. Many of our competitors are large apparel and sporting goods

companies with strong worldwide brand recognition, such as Nike, Inc., adidas AG, which includes the adidas and Reebok brands, and the Gap, Inc, which includes the Athleta brand. Because of the fragmented nature of the industry, we also compete with other apparel sellers, including those specializing in yoga apparel. Many of our competitors have significant competitive advantages, including longer operating histories, larger and broader customer bases, more established relationships with a broader set of suppliers, greater brand recognition and greater

Table of Contents

financial, research and development, store development, marketing, distribution and other resources than we do. In addition, our technical athletic apparel is sold at a price premium to traditional athletic apparel.

Our competitors may be able to create and maintain brand awareness using traditional forms of advertising more quickly than we can. Our competitors may also be able to increase sales in their new and existing markets faster than we do by emphasizing different distribution channels than we do, such as catalog sales or an extensive franchise network, as opposed to distribution through retail stores, wholesale or internet, and many of our competitors have substantial resources to devote toward increasing sales in such ways.

In addition, because we own no patents or exclusive intellectual property rights in the technology, fabrics or processes underlying our products, our current and future competitors are able to manufacture and sell products with performance characteristics, fabrication techniques and styling similar to our products.

Any material disruption of our information systems could disrupt our business and reduce our sales.

We are increasingly dependent on information systems to operate our e-commerce website, process transactions, respond to customer inquiries, manage inventory, purchase, sell and ship goods on a timely basis and maintain cost-efficient operations. Any material disruption or slowdown of our systems, including a disruption or slowdown caused by our failure to successfully upgrade our systems, system failures, viruses, computer hackers or other causes, could cause information, including data related to customer orders, to be lost or delayed which could especially if the disruption or slowdown occurred during the holiday season result in delays in the delivery of merchandise to our stores and customers or lost sales, which could reduce demand for our merchandise and cause our sales to decline. If changes in technology cause our information systems to become obsolete, or if our information systems are inadequate to handle our growth, we could lose customers.

If we encounter problems with our distribution system, our ability to deliver our products to the market and to meet customer expectations could be harmed.

We rely on our distribution facilities in Vancouver, British Columbia and Sumner, Washington for substantially all of our product distribution. Our distribution facilities include computer controlled and automated equipment, which means their operations are complicated and may be subject to a number of risks related to security or computer viruses, the proper operation of software and hardware, electronic or power interruptions or other system failures. In addition, because substantially all of our products are distributed from two locations, our operations could also be interrupted by labor difficulties, or by floods, fires or other natural disasters near our distribution centers. If we encounter problems with our distribution system, our ability to meet customer expectations, manage inventory, complete sales and achieve objectives for operating efficiencies could be harmed.

We are subject to risks associated with leasing retail space subject to long-term and non-cancelable leases.

We do not own any of our store facilities, but instead lease all of our corporate-owned stores under operating leases and our inability to secure appropriate real estate or lease terms could impact our ability to grow. Our leases generally have initial terms of between five and ten years, and generally can be extended only in five-year increments if at all. We generally cannot cancel these leases at our option. If an existing or new store is not profitable, and we decide to close it, as we have done in the past and may do in the future, we may nonetheless be committed to perform our obligations under the applicable lease including, among other things, paying the base rent for the balance of the lease term. Similarly, we may be committed to perform our obligations under the applicable leases even if current locations of our stores become unattractive as demographic patterns change. In addition, as each of our leases expire, we may fail to negotiate renewals, either on commercially acceptable terms or at all, which could require us to close stores in desirable locations.

Increasing labor costs and other factors associated with the production of our products in China could increase the costs to produce our products.

During fiscal 2010, approximately 60% of our products were produced in China and increases in the costs of labor and other costs of doing business in China could significantly increase our costs to produce our products and

Table of Contents

could have a negative impact on our operations, revenues and earnings. Factors that could negatively affect our business include a potential significant revaluation of the Chinese Yuan, which may result in an increase in the cost of producing products in China, labor shortage and increases in labor costs in China, and difficulties in moving products manufactured in China out of Asia and through the ports on the western coast of North America, whether due to port congestion, labor disputes, product regulations and/or inspections or other factors, and natural disasters or health pandemics impacting China. Also, the imposition of trade sanctions or other regulations against products imported by us from, or the loss of normal trade relations status with, China, could significantly increase our cost of products imported into North America or Australia and harm our business.

We may not be able to successfully open new store locations in a timely manner, if at all, which could harm our results of operations.

Our growth will largely depend on our ability to successfully open and operate new stores. Our approach to identifying locations for our stores typically favors street locations, lifestyle centers and malls where we can be a part of the community. As a result, our stores are typically located near retailers or fitness facilities that we believe are consistent with our customers' lifestyle choices. Sales at these stores are derived, in part, from the volume of foot traffic in these locations. Our ability to successfully open and operate new stores depends on many factors, including, among others, our ability to:

identify suitable store locations, the availability of which is outside of our control;

negotiate acceptable lease terms, including desired tenant improvement allowances;

hire, train and retain store personnel and field management;

assimilate new store personnel and field management into our corporate culture;

source sufficient inventory levels; and

successfully integrate new stores into our existing operations and information technology systems.

Successful new store openings may also be affected by our ability to initiate our grassroots marketing efforts in advance of opening our first store in a new market. We typically rely on our grassroots marketing efforts to build awareness of our brand and demand for our products. Our grassroots marketing efforts are often lengthy and must be tailored to each new market based on our emerging understanding of the market. Accordingly, there can be no assurance that we will be able to successfully implement our grassroots marketing efforts in a particular market in a timely manner, if at all. Additionally, we may be unsuccessful in identifying new markets where our technical athletic apparel and other products and brand image will be accepted or the performance of our stores will be considered successful.

If we fail to maintain the value and reputation of our brand, our sales are likely to decline.

Our success depends on the value and reputation of the lululemon athletica brand. The lululemon athletica name is integral to our business as well as to the implementation of our strategies for expanding our business. Maintaining, promoting and positioning our brand will depend largely on the success of our marketing and merchandising efforts and our ability to provide a consistent, high quality customer experience. We rely on social media, as one of our marketing strategies, to have a positive impact on both our brand value and reputation. Our brand could be adversely affected if we fail to achieve these objectives or if our public image or reputation were to be tarnished by negative publicity. Negative publicity regarding the production methods of any of our suppliers or manufacturers could

adversely affect our reputation and sales and force us to locate alternative suppliers or manufacturing sources. Any of these events could have a material adverse effect on our financial condition.

Our failure to comply with trade and other regulations could lead to investigations or actions by government regulators and negative publicity.

The labeling, distribution, importation, marketing and sale of our products are subject to extensive regulation by various federal agencies, including the Federal Trade Commission, Consumer Product Safety Commission and state attorneys general in the United States, the Competition Bureau and Health Canada in Canada, as well as by

Table of Contents

various other federal, state, provincial, local and international regulatory authorities in the countries in which our products are distributed or sold. If we fail to comply with any of these regulations, we could become subject to enforcement actions or the imposition of significant penalties or claims, which could harm our results of operations or our ability to conduct our business. In addition, the adoption of new regulations or changes in the interpretation of existing regulations may result in significant compliance costs or discontinuation of product sales and could impair the marketing of our products, resulting in significant loss of net sales.

Our fabrics and manufacturing technology are not patented and can be imitated by our competitors.

The intellectual property rights in the technology, fabrics and processes used to manufacture our products are owned or controlled by our suppliers and are generally not unique to us. Our ability to obtain intellectual property protection for our products is therefore limited and we currently own no patents or exclusive intellectual property rights in the technology, fabrics or processes underlying our products. As a result, our current and future competitors are able to manufacture and sell products with performance characteristics, fabrics and styling similar to our products. Because many of our competitors have significantly greater financial, distribution, marketing and other resources than we do, they may be able to manufacture and sell products based on our fabrics and manufacturing technology at lower prices than we can. If our competitors do sell similar products to ours at lower prices, our net revenue and profitability could suffer.

Our failure or inability to protect our intellectual property rights could diminish the value of our brand and weaken our competitive position.

We currently rely on a combination of copyright, trademark, trade dress and unfair competition laws, as well as confidentiality procedures and licensing arrangements, to establish and protect our intellectual property rights. We cannot assure you that the steps taken by us to protect our intellectual property rights will be adequate to prevent infringement of such rights by others, including imitation of our products and misappropriation of our brand. In addition, intellectual property protection may be unavailable or limited in some foreign countries where laws or law enforcement practices may not protect our intellectual property rights as fully as in the United States or Canada, and it may be more difficult for us to successfully challenge the use of our intellectual property rights by other parties in these countries. If we fail to protect and maintain our intellectual property rights, the value of our brand could be diminished and our competitive position may suffer.

Our future success is substantially dependent on the continued service of our senior management.

Our future success is substantially dependent on the continued service of our senior management and other key employees. The loss of the services of our senior management or other key employees could make it more difficult to successfully operate our business and achieve our business goals.

We also may be unable to retain existing management, technical, sales and client support personnel that are critical to our success, which could result in harm to our customer and employee relationships, loss of key information, expertise or know-how and unanticipated recruitment and training costs.

We do not maintain a key person life insurance policy on Ms. Day or any of the other members of our senior management team. As a result, we would have no way to cover the financial loss if we were to lose the services of members of our senior management team.

Our business is affected by seasonality.

Our business is affected by the general seasonal trends common to the retail apparel industry. Our annual net sales are weighted more heavily toward our fourth fiscal quarter, reflecting our historical strength in sales during the holiday season, while our operating expenses are more equally distributed throughout the year. As a result, a substantial portion of our operating profits are generated in the fourth quarter of our fiscal year. For example, we generated approximately 36%, 39% and 29% of our full year gross profit during the fourth quarters of fiscal 2010, fiscal 2009 and fiscal 2008, respectively. This seasonality may adversely affect our business and cause our results of operations to fluctuate, and, as a result, we believe that comparisons of our operating results between different quarters within a single fiscal year are not necessarily meaningful and that results of operations in any period should not be considered indicative of the results to be expected for any future period.

Table of Contents

Because a significant portion of our sales are generated in Canada, fluctuations in foreign currency exchange rates have negatively affected our results of operations and may continue to do so in the future.

The reporting currency for our consolidated financial statements is the U.S. dollar. In the future, we expect to continue to derive a significant portion of our net revenue and incur a significant portion of our operating costs in Canada, and changes in exchange rates between the Canadian dollar and the U.S. dollar may have a significant, and potentially adverse, effect on our results of operations. Additionally, a portion of our net revenue is generated in Australia. Our primary risk of loss regarding foreign currency exchange rate risk is caused by fluctuations in the exchange rates between the U.S. dollar, Canadian dollar and Australian dollar. Because we recognize net revenue from sales in Canada in Canadian dollars, if the Canadian dollar weakens against the U.S. dollar it would have a negative impact on our Canadian operating results upon translation of those results into U.S. dollars for the purposes of consolidation. The exchange rate of the Canadian dollar against the U.S. dollar has increased over fiscal 2010 and our results of operations have benefited from the strength in the Canadian dollar. If the Canadian dollar were to weaken relative to the U.S. dollar, our net revenue would decline and our income from operations and net income could be adversely affected. A 10% depreciation in the relative value of the Canadian dollar compared to the U.S. dollar would have resulted in lost income from operations of approximately \$5.7 million in the first two quarters of fiscal 2011 and approximately \$4.1 million in the first two quarters of fiscal 2010. Similarly, a 10% depreciation in the relative value of the Australian dollar compared to the U.S. dollar would have resulted in lost income from operations of approximately \$0.2 million in the first two quarters of fiscal 2011. We have not historically engaged in hedging transactions and do not currently contemplate engaging in hedging transactions to mitigate foreign exchange risks. As we continue to recognize gains and losses in foreign currency transactions, depending upon changes in future currency rates, such gains or losses could have a significant, and potentially adverse, effect on our results of operations.

The operations of many of our suppliers are subject to additional risks that are beyond our control and that could harm our business, financial condition and results of operations.

Almost all of our suppliers are located outside the United States. During fiscal 2010, approximately 4% of our products were produced in Canada, approximately 60% in China, approximately 26% in South and South East Asia and the remainder in the United States, Israel, Peru and Taiwan. As a result of our international suppliers, we are subject to risks associated with doing business abroad, including:

- political unrest, terrorism, labor disputes and economic instability resulting in the disruption of trade from foreign countries in which our products are manufactured;

- the imposition of new laws and regulations, including those relating to labor conditions, quality and safety standards, imports, duties, taxes and other charges on imports, as well as trade restrictions and restrictions on currency exchange or the transfer of funds;

- reduced protection for intellectual property rights, including trademark protection, in some countries, particularly China;

- disruptions or delays in shipments; and

- changes in local economic conditions in countries where our manufacturers, suppliers or customers are located.

These and other factors beyond our control could interrupt our suppliers' production in offshore facilities, influence the ability of our suppliers to export our products cost-effectively or at all and inhibit our suppliers' ability to procure certain materials, any of which could harm our business, financial condition and results of operations.

Our ability to source our merchandise profitably or at all could be hurt if new trade restrictions are imposed or existing trade restrictions become more burdensome.

The United States and the countries in which our products are produced or sold internationally have imposed and may impose additional quotas, duties, tariffs, or other restrictions or regulations, or may adversely adjust prevailing quota, duty or tariff levels. For example, under the provisions of the World Trade Organization, or the WTO,

Table of Contents

Agreement on Textiles and Clothing, effective as of January 1, 2005, the United States and other WTO member countries eliminated quotas on textiles and apparel-related products from WTO member countries. In 2005, China's exports into the United States surged as a result of the eliminated quotas. In response to the perceived disruption of the market, the United States imposed new quotas, which remained in place through the end of 2008, on certain categories of natural-fiber products that we import from China. These quotas were lifted on January 1, 2009, but we have expanded our relationships with suppliers outside of China, which among other things has resulted in increased costs and shipping times for some products. Countries impose, modify and remove tariffs and other trade restrictions in response to a diverse array of factors, including global and national economic and political conditions, which make it impossible for us to predict future developments regarding tariffs and other trade restrictions. Trade restrictions, including tariffs, quotas, embargoes, safeguards and customs restrictions, could increase the cost or reduce the supply of products available to us or may require us to modify our supply chain organization or other current business practices, any of which could harm our business, financial condition and results of operations.

Our trademarks and other proprietary rights could potentially conflict with the rights of others and we may be prevented from selling some of our products.

Our success depends in large part on our brand image. We believe that our trademarks and other proprietary rights have significant value and are important to identifying and differentiating our products from those of our competitors and creating and sustaining demand for our products. We have obtained and applied for some United States and foreign trademark registrations, and will continue to evaluate the registration of additional trademarks as appropriate. However, we cannot guarantee that any of our pending trademark applications will be approved by the applicable governmental authorities. Moreover, even if the applications are approved, third parties may seek to oppose or otherwise challenge these registrations. Additionally, we cannot assure you that obstacles will not arise as we expand our product line and the geographic scope of our sales and marketing. Third parties may assert intellectual property claims against us, particularly as we expand our business and the number of products we offer. Our defense of any claim, regardless of its merit, could be expensive and time consuming and could divert management resources. Successful infringement claims against us could result in significant monetary liability or prevent us from selling some of our products. In addition, resolution of claims may require us to redesign our products, license rights from third parties or cease using those rights altogether. Any of these events could harm our business and cause our results of operations, liquidity and financial condition to suffer.

Our founder controls a significant percentage of our stock and is able to exercise significant influence over our affairs.

Our founder, Dennis Wilson, beneficially owns more than 30% of our common stock. As a result, Mr. Wilson is able to influence or control matters requiring approval by our stockholders, including the election of directors and the approval of mergers, acquisitions or other extraordinary transactions. This concentration of ownership may have various effects including, but not limited to, delaying, preventing or deterring a change of control of our company.

Anti-takeover provisions of Delaware law and our certificate of incorporation and bylaws could delay and discourage takeover attempts that stockholders may consider to be favorable.

Certain provisions of our certificate of incorporation and bylaws and applicable provisions of the Delaware General Corporation Law may make it more difficult or impossible for a third-party to acquire control of us or effect a change in our board of directors and management. These provisions include:

the classification of our board of directors into three classes, with one class elected each year;

prohibiting cumulative voting in the election of directors;

the ability of our board of directors to issue preferred stock without stockholder approval;

the ability to remove a director only for cause and only with the vote of the holders of at least 66 $\frac{2}{3}$ % of our voting stock;

a special meeting of stockholders may only be called by our chairman or Chief Executive Officer, or upon a resolution adopted by an affirmative vote of a majority of the board of directors, and not by our stockholders;

Table of Contents

prohibiting stockholder action by written consent; and

our stockholders must comply with advance notice procedures in order to nominate candidates for election to our board of directors or to place stockholder proposals on the agenda for consideration at any meeting of our stockholders.

In addition, we are governed by Section 203 of the Delaware General Corporation Law which, subject to some specified exceptions, prohibits business combinations between a Delaware corporation and an interested stockholder, which is generally defined as a stockholder who becomes a beneficial owner of 15% or more of a Delaware corporation's voting stock, for a three-year period following the date that the stockholder became an interested stockholder. Section 203 could have the effect of delaying, deferring or preventing a change in control that our stockholders might consider to be in their best interests.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The following table provides information regarding our purchases of our common stock during the thirteen-week period ended July 31, 2011:

Period(1)	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs(2)	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs(2)
May 2, 2011 – May 29, 2011	5,422	\$ 45.76	5,422	5,650,224
May 30, 2011 – July 3, 2011	5,207	47.37	5,207	5,645,018
July 4, 2010 – July 31, 2011	4,186	60.86	4,186	5,640,831
Total	14,815		14,815	

(1) Monthly information is presented by reference to our fiscal months during our second quarter of fiscal 2011.

(2) Our Employee Share Purchase Plan (ESPP) was approved by our Board of Directors and stockholders in September 2007. All shares purchased under the ESPP are purchased on the Toronto Stock Exchange or the Nasdaq Global Select Market (or such other stock exchange as we may designate from time to time). Unless our Board of Directors terminates the ESPP earlier, the ESPP will continue until all shares authorized for purchase under the ESPP have been purchased. The maximum number of shares authorized to be purchased under the ESPP is 6,000,000.

ITEM 6. EXHIBITS

Exhibit No.	Exhibit Title	Filed Herewith	Incorporated by Reference		Filing Date
			Form	Exhibit No. File No.	
31.1	Certification of Chief Executive Officer Pursuant to Exchange Act Rule 13a-14(a)	X			
31.2	Certification of Chief Financial Officer Pursuant to Exchange Act Rule 13a-14(a)	X			
32.1	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	X			

Table of Contents

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.

lululemon athletica inc.

By: /s/ John E. Currie

John E. Currie
Chief Financial Officer
(Principal Financial Officer and
Principal Accounting Officer)

Dated: September 8, 2011

Table of Contents

Exhibit Index

Exhibit No.	Exhibit Title	Filed Herewith	Incorporated by Reference		Filing Date
			Form	Exhibit No. File No.	
31.1	Certification of Chief Executive Officer Pursuant to Exchange Act Rule 13a-14(a)	X			
31.2	Certification of Chief Financial Officer Pursuant to Exchange Act Rule 13a-14(a)	X			
32.1	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	X			