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Q1 2023 Earnings Call

Company Participants

- Bracken Darrell, President and Chief Executive Officer
- Nate Melihercik, Head of Global Investor Relations
- Nate Olmstead, Chief Financial Officer

Other Participants

- Adam Angelov, Analyst
- Alex Duval, Analyst
- Ananda Baruah, Analyst
- Asiya Merchant, Analyst
- Erik Woodring, Analyst
- Joern Iffert, Analyst
- Michael Foeth, Analyst
- Paul Chung, Analyst
- Serge Rotzer, Analyst
- Torsten Sauter, Analyst

Presentation

Nate Melihercik {BIO 20814398 <GO>}

Good morning and good afternoon. Welcome to Logitech's Video Call to discuss our Financial Results for the First Quarter of Fiscal 2023. Joining us today are Bracken Darrell, our President and CEO; and Nate Olmstead, our CFO.

As a reminder, during this call, we will make forward-looking statements, including with respect to future operating results under the Safe Harbor of the Private Securities Litigation Re Act of 1995. We're making these statements based on our views only as of today, and our actual results could differ materially. We undertake no obligation to update or revise any of these statements. We will also discuss non-GAAP financial results, and you can find a reconciliation between non-GAAP and GAAP results and information about our use of non-GAAP measures and factors that could impact our financial results in our press release and in our filings with the SEC, including our most recent annual report and subsequent filings. These materials as well as our prepared remarks and slides and a webcast of this call are all available at the Investor Relations page of our website.

We do encourage you to review these materials carefully. Unless otherwise noted, comparisons between periods are year-over-year and in constant currency and sales are

net sales. And finally, this call is being recorded and will be available for a replay on our website.

And with that, I will now turn the call over to Bracken. Good morning, Bracken.

Bracken Darrell {BIO 3403495 <GO>}

Thank you, Nate, and thanks all of you for joining us. Logitech, like many other companies is experiencing the impact of a wide range of overlapping macroeconomic and geopolitical issues. The war in Ukraine directly reduced our net sales about 2% versus last year, as we talked about earlier. Foreign currency headwinds have increased with the dollar strengthening to nearly 1:1 in the year amount [ph]. Inflation rose further and consumer confidence has weakened. None of these fundamentally affect our optimism for our target markets, our strategy or our business model.

But as we look at the quarter and ahead into the rest of the year, we believe it's prudent to take a more conservative view than we had previously. Impacted by these challenges, our net sales were down 9% in constant currency this quarter. There were clear highlights for sure, solid growth in Video Collaboration, Keyboards & Combos and Pointing Devices as hybrid and return-to-work trends continue to take shape. We grew market share and we delivered solid gross margins of 40% despite worsening inflation and currency impacts.

As I just said, our overall net sales in Q1 combined with the worsening macroeconomic picture made us take a hard look at our assumptions for the rest of the fiscal year. We can't affect currency exchange rates or inflation, of course, but we can adjust our business to the current conditions. And although we can't predict the depth and duration of these macroeconomic conditions, we can conservatively manage our business until we have evidence that the markets will return to stronger growth.

In short, we can't change the macros, but we can adjust to them. And that's what we're doing. Based on current conditions and performance, we're implementing plans to reduce operating expenses by approximately 10% or about $150 million versus last year, predominantly through variable cost reductions. As our sales nearly doubled since fiscal year '20, we had a disproportionately variable cost, which makes us ready to meet the moment. We'll continue to raise prices to offset the currency and inflation and target to keep a strong margin profile.

We'll continue to invest in exciting new innovative products. This investment has been a key driver of our sustained share gains and we believe it will be into the future. All that's leading us to provide you with an updated outlook for fiscal year '23, by reducing expectations for both revenue and operating profit. We believe this update appropriately takes into account the macroeconomic and geopolitical environment we are in, as well as our own plans to lower costs and take control all the variables within our graphs.

Before I let Nate take you through our financials and outlook in more detail. Let me just say at the macro picture we're dealing with now is challenging, but we believe it's

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temporary. I'm as optimistic as ever about the long and -- the medium and long term. I can't think of anywhere I'd rather be for the long term and writing the secular trends Logitech gives. Hybrid work or the idea of work from anywhere is simply a future. As I've said a few months ago, the debate is over, hybrid won, and that will favor Logitech as offices [ph] are renewed for new footprints and more video, and homes continue to upgrade for better offices.

While the gaming market was softer over the past two quarters, we believe the interest in gaming will increase over the long term as gaming content expands, cloud gaming grows and more and more people become gamers socially or even competitively. And the streaming and content creation trend will grow and grow. From individual creators producing content from home to businesses leveraging podcasts and creators for to new markets. The use of streaming content continues to expand driving growth of this trend.

So we're going to continue to focus on great long-term growth but run the business conservatively short term. What does that mean? Our product teams across our largest businesses Video Collaboration, C&P and gaming, we'll continue to launch a series of new products throughout the remainder of the year. As in the past, you can expect these products to be packed with the innovative features, full of lifestyle design enhancements and critical to the work and play of both consumers and enterprises. Our operations team will continue to optimize our supply chain for the short and long-term as we source components from a diversified set of vendors now much more diversified, adjust shipping [ph] routes, and mitigate transportation costs and risks and finally, diversify manufacturing outside of China. We all been working hard to flip the inflationary trend to cost reduction as the macroeconomic type turns and it always turns.

Our sales teams, especially our enterprise teams will continue to refine and improve their go-to-market capabilities across the globe. And will go all out to help companies reconfigure offices, expand the video enablement and create workspaces appropriate to this hybrid world. We will bring down expenses significantly to align with the market realities that we project for the fiscal year. And as we do this, we'll focus on organizing for maximum effectiveness over the next few years.

Our capital allocation priorities remain unchanged. Investment in our product design and development capabilities, accretive M&A and returns on capital to shareholders in the form of share repurchases and dividends. And finally, you can expect our commitment to sustainability to remain firmly in place. We were just named by EcoVadis as one of the top 1% of sustainability companies in the world. And our plan is to turn sustainability into a driver for good and for growth will continue.

Now let me turn the call over to Nate for breakdown of our financial performance this quarter and our new outlook. Nate?

Nate Olmstead {BIO 21036514 <GO>}

Thanks, Bracken. Bracken described our perspective on the quarter and environment, it signals that we need to be prudent about the rest of the year or until economic trends

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become more consistent and favorable. I'll spend a few minutes on the quarter and then walk you through our updated outlook. In Q1, net sales were down 9% to $1.16 billion, after growing 58% in Q1 of last year. We grew in Video Collaboration, Keyboards & Combos and Pointing Devices while facing tough compares in the macro environment.

Gross margins remained essentially flat sequentially despite the litany of external factors the pressured profitability. I mentioned last quarter that cost increases, unfavorable currency rates, and higher shipping rates may pressure half one fiscal '23 margins. And while we did see these impacts, we managed pricing and reduced our reliance on air freight to help offset these pressures. However, we anticipate Q2 margins will be lower than Q1 as these headwinds remain. Operating profit was down as expected after doubling last year. Cash from operations was negative $36 million, also as expected, and an improvement of $79 million versus Q1 last year.

Let's review some of the results across our product categories. Similar to last quarter, the gaming market continued to decline in Americas and Europe, while growing in Asia and our results reflected these trends with sales down 13% globally. We outperformed the market, however, and gained PC gaming share. We saw a momentum from our products geared toward both social and professional gamers offset by ongoing headset demand weakness in core PC and console gaming.

Video Collaboration sales increased 7% as conference room cameras and systems grew double-digits to more than offset double-digit declines in business oriented webcams, which are part of our video collaboration category. In creativity and productivity, Keyboards & Combos grew 7% and Pointing Devices were up 3%. We saw solid and consistent demand during the quarter for PC peripherals and introduced a series of new products. Our Master Series line added two mechanical keyboards and an upgraded mouse, and we also released a line of keyboard combos to support our enterprise customers.

Taken together, these results highlight the performance of our categories addressing the secular trends in Gaming, Video Collaboration and Hybrid Work. Sales of our creativity and productivity Gaming and VC products exceeded 80% of our total net sales this quarter, and were flat year-over-year in constant currency. If you exclude Russia, these categories actually grew 2%. We have growth opportunities in other categories as well. But I wanted to highlight the performance of these key areas that directly address the strategic secular trends that Bracken referenced.

Looking regionally, Asia-Pacific grew nicely in the quarter driven by Gaming, while Americas and EMEA sales declined. Through the excellent work of our operations and sales teams, we were largely able to recover from the COVID lockdowns in China. For those that track the sell-in and sell through data in our earning slides, you can see that globally these metrics are in balance. The timing of the Shanghai reopening, however, resulted in the bulk of our China sales occurring later in the quarter, which is why Asia sell-in was stronger than sell-through.

Turning to expenses. I mentioned last quarter that we wouldn't hesitate to reduce our variable expenses including marketing if conditions warranted. Given the weaker top line

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results that is what we did in Q1. We reduced marketing and sales spend by 10% and reduced G&A by 9%. We've also said that investment in product design and development would remain a priority for Logitech even during trying economic times, and you'll note that we increased R&D investment by 9%.

We are not done on reducing or eliminating unproductive expenses from our business and we are driving efficiency in all our spend, including fixed cost, product and freight costs and our go-to-market investments in the channel. We can't offset every headwind that we predict for this year, but we are taking aggressive actions to align our spend with our sales while sustaining an investment we believe supports our longer term growth ambitions.

We ended the quarter with a cash balance of approximately $1.1 billion after returning nearly $121 million in capital to shareholders through our share repurchase program. As a sign of our confidence in cash generation and our commitment to returning cash to shareholders, our Board approved an increase in our repurchase authorization by another $500 million and we proposed a 10% increase to our dividend per share for approval at our September Annual Meeting.

Finally, I'll spend a minute on our updated fiscal year '23 outlook. In May, we provided an annual outlook of 2% to 4% growth in constant currency and an operating profit outlook of $875 million to $925 million. Since that time, we've seen continued and in some cases intensified deterioration of economic conditions across the globe. Bracken discussed the external environment earlier. So when we developed this new outlook, we made assumptions about a number of factors including potentially protracted economic volatility and sustained revenue and profit pressure from the stronger US dollar.

Given these considerations and the actions we are taking to reduce cost versus last year, we now expect full-year revenue to be down 4% to 8% in constant currency and full year non-GAAP operating income to be between $650 million and $750 million. At the midpoint, our outlook for profit is down $200 million versus our prior estimates. At a high level that comes through two headwinds and two partial offsets.

The headwinds totaled about $400 million, including approximately $250 million of reduced profit from lower volumes and cost increases and $150 million of lower profit from currency changes, offsetting these unfavorable impacts are OpEx reductions and pricing. So in summary, we see about $400 million of incremental profit headwinds for the full year of which we have plans to offset 50% through actions we are taking.

Nate, we can open the line for questions. Thank you.

Questions And Answers

A - Nate Olmstead {BIO 21036514 <GO>}

Great. Thank you, Nate. (Operator Instructions) We'll start with Paul Chung from J.P. Morgan. Good morning, Paul.

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Q - Paul Chung {BIO 20654199 <GO>}

Hi, good morning. Good to see you guys.

A - Bracken Darrell {BIO 3403495 <GO>}

You too.

Q - Paul Chung {BIO 20654199 <GO>}

Thanks for taking my question. So VC and Keyboards were kind of a nice bright spot in a tough quarter. And in VC, you're kind of seeing some relative strength and conference cam. So, were you seeing demand across verticals, regions, is this for new conference rooms kind of replacement of legacy competitors? Any update you have there seeing in terms of competition as well?

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah, I mean, the conference cam number was strong. I mean, I think we put it in the script, the conference cam number grew very strong double-digits this quarter.

Q - Paul Chung {BIO 20654199 <GO>}

Double digit. Yeah.

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah. And it was about what you would have expected, I mean, it was pretty much a global story, the Americas, in particular, were very strong. And I think that's the kind of reflects this or the return to work that's happening here in the West. You want to add anything to that Nate?

A - Nate Olmstead {BIO 21036514 <GO>}

Yeah, I think it was pretty consistent, Paul, and the sell through has remained pretty consistent actually going back several quarters. You know, it's been a little bit tough to predict sometimes on the sell-in because of the start and stop nature of some of the reopening. But if you just look at the sell-through, another quarter of double-digit sell-through as well as net sales.

Q - Paul Chung {BIO 20654199 <GO>}

Got it. And then on capital allocation, so the pace of buybacks has been quite elevated over the last four quarters. The increase in authorization, so just kind of more of the same over the next 12 months, maybe at a similar pace or higher pace, is that the right way to think about it? And then separately, private market valuations looking more attractive today from your seat where you're seeing opportunities there? Thanks.

A - Nate Olmstead {BIO 21036514 <GO>}

Let me take the buyback here. I think, Paul, really I think about this is the Board gave us the option to increase repurchases, but I would just think about it as we're seeing consistent

to our strategy around capital allocation, right. We still prioritize investing in the business. And then from there we have a balanced approach really on dividends and share repurchases. In fact, if you look back over the last several years, going back to FY'20, we've returned about $1.3 billion to shareholders through repurchases and dividends, and that's been roughly 50-50, a little bit more weighted to our share repurchases, to your point recently, I think about 60% over that time share repurchases. But we are confident we'll continue to generate cash and we think it's great to have that option.

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A - Bracken Darrell {BIO 3403495 <GO>}

Yeah, I'll just add, first of all, I'm really thankful to the Board for giving us the increase in the authorization, I feel really good about the buyback program we've got going. In terms of M&A, we never stopped on M&A, we were aggressively going after whatever we saw available. We did -- nothing really stopped us from a valuation standpoint before. But you're right, I mean, there is no doubt that valuations have come down across the board. So we've always got a lot of activity going. We have a lot of activity going now. So it's not going to let up.

Q - Paul Chung {BIO 20654199 <GO>}

Thank you.

A - Nate Olmstead {BIO 21036514 <GO>}

Thanks, Paul.

A - Bracken Darrell {BIO 3403495 <GO>}

Thanks, Paul.

A - Nate Melihercik {BIO 20814398 <GO>}

Thanks, Paul. Next up will be Asiya Merchant from Citi. Hi, Asiya.

Q - Asiya Merchant {BIO 20247269 <GO>}

Hey, good morning, everyone.

A - Bracken Darrell {BIO 3403495 <GO>}

Good morning.

Q - Asiya Merchant {BIO 20247269 <GO>}

Good question. For the guidance that you guys are providing, I guess the question is, if you can help us understand through each of the categories. What's kind of baked in, is this the worse that it gets? And if you can kind of walk us through how the minus 8 to minus 4 makes sense in the current environment? It's suggests that it will improve from here on. Is that just a function of easier comps through the rest of the year? Or -- and if you can walk us through some of the categories, that would be great. Thank you.

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A - Bracken Darrell {BIO 3403495 <GO>}

Nate, why don't you take the first part of that, and then I'll come in at the back and talk more about categories.

A - Nate Olmstead {BIO 21036514 <GO>}

Okay. I was going to start with categories. No, I'm just -- so Asiya, I think early the year, you can always look at it year-over-year, you can get it quarter-over-quarter. Let me try to explain to you a little bit about how I thought about it quarter-on-quarter. What the outlook reflects is that we don't think that we've seen the -- every bit of bad news yet. And Q2 will be softer than what it has been historically. Normally, we see an increase sequentially from Q1 to Q2 in kind of the mid-teens on growth, the outlook sort of reflects that it's probably mid-single digits. So Q2 is not going to see the same spike that it has before. And that's sort of a continuation of some of the trends that we saw in Q1. And then from there, if you think about the range that we have for the full year, the 4% to 8%, really the difference there is how we think about the holiday and the back half of the year.

So at the low end of the range, I think the holiday is a little bit weaker than typical seasonality at the high end of the range. We're starting to get back to typical seasonality in the back half. That's what it really reflects. As Q2, our outlook reflects a weaker than normal seasonality in the back half of the year, depending on which end of the range you talk about kind of at the midpoint, still weaker than normal seasonality in Q3 and then some return to normalcy in Q4. And then to your point on the year-over-year compares, that just comes down to some easier compares. So that's how I think about it sequentially.

A - Bracken Darrell {BIO 3403495 <GO>}

Yes, I'll just add categories, you can jump back in, Nate. I think we're -- I think from a category standpoint, we -- our view is about the same as what you see this quarter. And we think we're going to continue to have a pretty good workspace business, mice and keyboards We're actually constrained a little bit. We're still constrained a little bit on mice, which shows up both in the mouse and the keyboard business. So I think that's going to continue to be a solid business for us. And of course, the VC business conference room, we think conference rooms are going to continue to be enabled. That's a good thing. We think the Gaming business pullback is probably going to stay pull back. I don't think it will get. We don't expect a big change in that we think it will pull back.

Now all that said, we just finished Prime Day. This year, Prime Day was in Q2. So -- and last year was in Q1. Our Prime Day was up 24% versus your guide I think, Nate. So that's in constant currency. That's in dollars, by the way. So it's not all a pullback here. I mean there's still plenty of interest in our categories. I think that's kind of a good reflection of the future. But I do think it's prudent for us to really look at the world the macroeconomic what we're looking at and just moderate across most of our categories in light of what's happening.

A - Nate Olmstead {BIO 21036514 <GO>}

Yeah. And just to kind of re-highlight something I mentioned in my prepared remarks, Asiya, that those four categories that I talked about, Gaming, Video Collaboration,

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Keyboards & Combos and Pointing Devices, those are the ones that are predominantly addressing the secular trends that we talk about so often. Over 80% of our net sales this quarter combined those categories were flat. They grew if you exclude the impact of Russia. So -- and that's with the gaming decline, right, of 13% in there. So it does indicate some durability, if you will, or continued interest in those categories, which I think is very healthy.

Q - Asiya Merchant {BIO 20247269 <GO>}

Okay. And then capital still remains kind of high at $110 million. I know you guys talked about the variable cost structure and being able to manage that. Anything on CapEx and why you guys are keeping that at a high level, relative to where you guys have been in fiscal -- the last fiscal year, for example?

A - Nate Olmstead {BIO 21036514 <GO>}

Yeah. I mentioned this before. What you see here is the catch up this year, some investments in facilities. Over the past couple of years, as offices have been closed, we haven't been making investments or expanding footprints. And as we've invested in our headcount and in our people, we have the need to invest in CapEx this year. So the increase that you see this year is predominantly into facilities, not necessarily a new run rate, but we have some catch-up to do because it's been low the last couple of years.

Q - Asiya Merchant {BIO 20247269 <GO>}

Okay. All right. Thank you.

A - Nate Melihercik {BIO 20814398 <GO>}

Thanks. Our next question will be from Torsten Souter from Kepler Cheuvreux. Torsten, good morning, good afternoon.

A - Bracken Darrell {BIO 3403495 <GO>}

Hey, Torsten.

Q - Torsten Sauter {BIO 6588509 <GO>}

Hello, everyone. Thanks for taking my questions. Actually, I have two. First, is it fair to assume that you can cut the OpEx by, say, USD150 million, USD200 million if needed. And if so, where could you cut without hurting the franchise? And then if I may, secondly, I wonder to what extent has the deliberate direct B2B sales channel for Video Collaboration also supported and catalyzed sales in other categories. In other words, how much non-VC products are you selling in this deliberate enterprise channel?

A - Bracken Darrell {BIO 3403495 <GO>}

Let me take the second one, and Nate, I'm going to let you take the first one. I would say not much yet. The direct enterprise sales force has been, we really organized to focus completely on the ConferenceCam business. And in fact, I used to say for years, I would say, I really don't want to hear the word mouse come out of anybody's mouth in the

enterprise sales force because we're really good at mice, and we need to get good at ConferenceCam. Boy, that's changed. We're now at the point where I feel like we're -- we've got to build a big structure at enterprise sales force where that I feel good about. And I think now we're ready to add to it. So we're in the very early days of taking advantage of that for the rest of our business. But we are seeing large sales through there already, but it's still very early days.

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A - Nate Olmstead {BIO 21036514 <GO>}

And then on your question on OpEx, that is our plan, is to reduce spend year-over-year in OpEx $150 million. We've talked about it before. As we've invested over the past few years, we've invested both in fixed and variable costs, but the majority of it actually in variable cost, Torsten. So I think we've been prepared for such a time like this where we have to reduce those expenses, and so we'll go execute those plans.

Also, it's important probably keep in mind, OpEx is not the biggest portion of our spend in the company. We spent about $3 billion in cost of sales. And so we're looking at all areas of spend. So there's $4.5 billion of spend that I really go after and look at and make sure we're spending wisely and efficiently, looking for opportunities. Now all that spend is different, and you got to think about it uniquely. And in this environment where we've seen cost pressure and cost of sales, it's difficult to reduce it, but we still need to make sure that we optimize it. So we're not focused just on one piece of it. We're looking at all of it.

Q - Torsten Sauter {BIO 6588509 <GO>}

Very clear. Thanks.

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah. Thanks, Torsten.

A - Nate Melihercik {BIO 20814398 <GO>}

Our next question will be from Joern Iffert from UBS.

A - Bracken Darrell {BIO 3403495 <GO>}

Hello, Joern.

Q - Joern Iffert {BIO 15374623 <GO>}

Hi. Hi. I cannot switch on my video. The host is not allowing it. So I have to just ask questions acoustically. Maybe the first question is, please, on the guidance again for portfolio, the minus 8% to minus 4%. Can you help us understand what is the FX impact? What is roughly the volume impact? What are the price impacts that we can better read underlying trends? Maybe I'll take the question, one of mine [ph] and stop with this one, if I may.

A - Nate Olmstead {BIO 21036514 <GO>}

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Okay. Sure. Well, the straight volume impact, if you will, if you went to the midpoint to midpoint, you are -- we were at plus 3% constant currency and midpoint now minus 6%. So there's a 9-point swing there, excluding the impacts of currency, as you can think about as volume. And then the currency impact itself increased by about 3 points. So we had about a 1-point currency impact. That's now gone to 4 points for the year. So the spread between US dollar and constant currency growth is expected to be about 4 points versus just 1 point previously.

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Q - Joern Iffert {BIO 15374623 <GO>}

And on pricing versus volumes?

A - Nate Olmstead {BIO 21036514 <GO>}

Yes. So if you flow that through to -- and I kind of mentioned this in my prepared remarks, if you flow through that volume impact down to profit, it's about -- the problem -- one of the big problems of currency is flow through at a very high rate, right? Because our cost of goods are primarily in US dollars. So when we have an unfavorable currency impact flows through at a very high rate to operating profit. Frankly, if things reverse, the opposite is true, it flows through to very high rate favorably to profit.

So that currency flow-through, which about 3 points, you can think of it's about $175 million of currency pressure on the top line. That flows through at a very high rate now right down to profit. That is one of the reasons why we've taken some pricing actions because normally, our strategy when currency moves unfavorably, would be to do that. So we've taken some pricing actions to help offset some of that. But then you've also got the volume impact as well from weaker demand in many of those macroeconomic factors, which flows through. And that demand side, 9 points, like I mentioned, about $475 million, $500 million of volume flowing through. We can offset more of that and that flows through at more traditional rates, but it's a combination of the OpEx and the pricing actions we've taken that are offsetting those volume and currency impacts that I mentioned.

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Q - Joern Iffert {BIO 15374623 <GO>}

Okay. Second question, please, on the $200 million recycling savings out of the $400 million incremental negative impact on non-GAAP EBIT. Can you help us to provide a really more clarity? Where exactly this $200 million recycling is coming from or costing is coming from and little bit concrete examples?

A - Nate Olmstead {BIO 21036514 <GO>}

Yeah. So the $200 million, about three-fourths of that will be the OpEx reductions. I mentioned, $150 million year-over-year and the other $50 million from pricing. The OpEx is very easy to measure. We know where all those are the pricing. We've got to make some assumptions about what the impact is on volume and so forth, but that looks like what our capture rate is. We put those increases in a little later in the year. So I think have pretty good visibility to what that is. But the OpEx will primarily come out of variable expense, and a lot of that will come out of variable marketing as we've talked about. But there's other areas that we're looking at to and have plans to reduce again, mostly on the

variable side, very similar to what we've been talking about for the last few quarters actually.

Q - Joern Iffert {BIO 15374623 <GO>}

And the last question, if I may, in terms of the end markets. And speaking about gaming, for example, do you see that consumer sales trends have stabilized recently after the weakening over the last couple of months or it's still in a declining mode and you do not know exactly when the trough is materializing open gaming.

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah. I would say it's -- we're in the middle of the summer. I don't know if you can remember what you were doing last summer at this time, but I know I can't because I didn't do anything interesting. This summer, everybody is traveling, whether you're in Europe or maybe except for China, everybody is on the move. So the -- I'd say the trends are really tough to read right now in Gaming. It's a very soft Gaming market. Now when they come back -- when people come back in the fall and if you just think about it, you have a 12-week summer and you're traveling two or three weeks of it. That's a very different picture.

So it's really hard for us to extrapolate from what we're seeing this summer to -- in the middle of the summer right now to what's going to happen in the rest of the year. But I would say, I think the reality is that we're going to have a Gaming market that will be down for the year. And probably significantly down like we're seeing right now. And really the key question is, when does that start to recover? It will recover. And I think it's going to be as we get further into the back half of the year.

Q - Joern Iffert {BIO 15374623 <GO>}

All right. Thanks a lot.

A - Bracken Darrell {BIO 3403495 <GO>}

Thank you, Joern.

A - Nate Melihercik {BIO 20814398 <GO>}

Thanks, Joern. Our next question will be from Alex Duval at Goldman Sachs. Hey, Alex.

A - Bracken Darrell {BIO 3403495 <GO>}

Hey, Alex.

Q - Alex Duval {BIO 16682293 <GO>}

Thanks very much for the question. If we look at the lower top line guidance that you put out today as well as the altered EBIT guidance, it looks like you're assuming around $0.60 of EBIT loss for every lost dollar revenue. But of course, we know that your group gross margin would be closer to 40%. So I wondered if you could just talk a little bit to the drop-through that you're assuming? How come it's so high given that, obviously, you're taking

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some cost out? And I wondered, is that because you're baking in an expectation of further pricing pressure so as to clear out inventories? So how should we be thinking about that? And then I have a quick follow-up.

A - Nate Olmstead {BIO 21036514 <GO>}

The primary reason, Alex, why you'd see a higher flow-through is because currency is a big portion of that, right? I said there's about $175 million of incremental currency pressure on the top line and that flows through at almost 100%, we can offset some of that. And again, that's gross, excluding the impact of pricing. So you can think about which headwind you want to use the pricing as an offset to when you think about the math. But the real reason why the high flow-through is going to be currency.

Q - Alex Duval {BIO 16682293 <GO>}

Very, very clear. I appreciate that. And then some investors have also been asking, even with the new guidance, obviously, your revenues and EBIT would still be at a level significantly higher than pre-pandemic. So to what extent at the moment, are you at all concerned about a mean reversion to where you were beforehand? Is the risk more about sort of consumer demand at the moment? Or are you sort of seeing signs of any of these categories of a pull forward and sort of anything that would prompt you to kind of reassess your thesis that these are more structural trends that will endure for the long term?

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah, right now, I wouldn't say we see anything that would suggest that our -- the structure or secular trends that we've been seeing are going to slow down. This period of kind of adjustment this temporary period. It feels like a temporary period. If you just go through each one of them, the hybrid work trend, and we're still only one-tenth of all the conference rooms enabled our ConferenceCam number is growing strongly. And I think we're still -- and if you talk to companies around the world, so many of them, including us, are really looking at their footprints and trying to decide what are we going to do? And we've landed our plane now. We kind of know what we're doing around the world, but a lot of companies really have it yet.

If you go into workspaces, just the number of workspace has increased so significantly that the replacement rate, the sheer replacement rate on upgrading workspace is it looks like kind of what it did pre-pandemic just a lot more of them. And there's a lot more upgrading to do because you have a different dynamic. It's part of your home decor, it's -- you're kind of living with it all day long. So -- and you're going to be working in the home and some of the office too. So -- and then there's Gaming. And Gaming, absolutely as much confidence as ever on the Gaming business. There are companies like Microsoft or more and more of the large meta who are coming into the Gaming space. They're investing in the Gaming space because Gaming is going to be a very, very long-term strong growth engine, and that's what drives our business, the investment in content, the creation of new compelling things. This generation is below. So I wouldn't -- I definitely don't think anybody should be overreacting to what's happening in Gaming right now. I do think you've got had a very, very strong two years of Gaming. And now you've got a lot of

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people who are back out again and doing other things and spending their money on trips and totally get it and getting back out. But I think the secular trends will continue.

A - Nate Olmstead {BIO 21036514 <GO>}

And I will comment on Gaming, I think specifically, Alex, if we went back and looked at our Analyst Day a couple of years ago, so this is -- I thought the Gaming market or our Gaming business might be kind of flat year-over-year after a really strong FY'21 at plus or minus 5%. We ended up growing 17% last year. And -- but the thinking back then was, hey, listen, as things reopen, there'll be some substitution effect, other forms of entertainment. We'll probably see Gaming take to slow down a bit. And I think what I'm seeing right now is I think that that's taken another year from what I thought originally, right?

The things didn't really reopen last year like they thought -- we thought they would. But we're seeing that now. A lot of the weakness that we see and that I see in the market isn't in headsets. Be clear, all the other categories have declined as well, but headsets in particular, have been down a lot. And certainly, on the console side, we know that some of that is due to shortages and timing of title releases and things like that shortages on consoles themselves. But I think also some of the headset demand probably during the past couple of years was from non-gaming use as well. People using buying headsets, using them for Zoom calls and hybrid work. So not unexpected to see some particular pressure, I think, in that category. But for the reasons Bracken mentioned, I think the fundamental drivers of the Gaming industry remains strong.

Q - Alex Duval {BIO 16682293 <GO>}

Thanks a lot.

A - Nate Olmstead {BIO 21036514 <GO>}

Sure.

A - Bracken Darrell {BIO 3403495 <GO>}

Thank you.

A - Nate Melihercik {BIO 20814398 <GO>}

All right. Next up will be Erik Woodring from Morgan Stanley. Good morning, Erik.

A - Bracken Darrell {BIO 3403495 <GO>}

Hi, Erik.

Q - Erik Woodring {BIO 19492555 <GO>}

Hey, good morning guys. So maybe Bracken, I'll pose one to you and then one to Nate. As we move kind of further into this kind of post-COVID hybrid work environment. Obviously, you own a number of the markets you're establishing mice, keyboards, webcams, headsets. How should we think about your desire to enter new or adjacent markets or

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maybe accelerate investments into markets like music where you can regain a firmer hold on the share that you once had, kind of obviously all in a request, all in the goal to get back to kind of that 8% to 10% growth range. Just curious how you think about that question.

A - Bracken Darrell {BIO 3403495 <GO>}

We're always looking at new categories, Erik. Since I've been here, I think we've gone from about a little over a dozen categories to over 25 or 30 now. So -- and so we've got things in development all the time to try to go into new categories. We really try to start the seed [ph] programs first and then we'll acquire something if it makes sense to either augment that accelerated to replace it. So we're going to keep doing that. And I would say we've done actually quite a bit of category expansion in the enterprise space. And I think that is a good opportunity for us. We've gone in the cabling, into whiteboard cameras and into meeting room screens. And so we -- and we'll continue to look across the whole business at that, to your point. The music business, in particular, we talked about really pulling back on the Bluetooth speaker business because we just didn't love the fundamentals of that business. And I still feel the same way about that. I don't think you'll see us like doubling down on that. We're still in it. It's still a great contributor in many ways. But I don't think that's a space we look at, but we see spaces across the board to keep expanding.

But the good news is, I really think the fundamentals of our current categories can deliver that long-term guidance we talked about already. I mean, the fundamental growth opportunity in conference rooms, the workspace opportunity. When I came here, I never would have dreamed that we'd have the kind of growth opportunity we have in mice and keyboards that we have now ahead of us. And of course, Gaming, we just spent time talking about.

And the only other thing we haven't talked about is the streaming and creating phenomenon. It's super exciting. I mean if you just think -- most of you are not in the flow of discussions on what's the future of marketing. And a lot -- what many of us would say the future of marketing is it will be disproportionately large for creators themselves where they'll actually be selling, transacting or a minimum directly, strongly influencing the sale. And those are -- and that's aspirational for all of our kids and everybody under the age of 30. So many people want to be a streamer creator. So we're in all those spaces. And there's a lot of growth ahead in all of them.

Q - Erik Woodring {BIO 19492555 <GO>}

Okay. That's helpful. Thank you, Bracken. Maybe one to you, Nate. So sales and marketing down, call it, 10% in the June quarter. You've alluded to containing variable costs. of which sales and marketing, I assume, is a sizable chunk of that. How does a pullback in those efforts impact your need to discount products? And any way you can kind of help us think about the impact of discounting in fiscal '23 on kind of your net sales growth outlook that you provided last night?

A - Nate Olmstead {BIO 21036514 <GO>}

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Sure. Why don't I start with this one, and Bracken, you may want to comment a little bit too on the marketing strategies. We've seen some pockets, Erik, not unexpected where promotional activity has increased, but that's really we're sticking with our strategy, which is really to drive marketing even at lower levels of marketing investment drive marketing to increase the value of the brand and to drive preference for Logitech without having to be so promotional. And that's really our -- it's been our long-term strategy, and we're continuing to do that even during this year.

Now I think, again, as gross margins have come down for some of the, I think, more temporal reasons that we've talked about before, cost increases, logistics rates increases, now currency, that's put some pressure on the cost structure. And so the place that we're going to go address that right now is with variable spend. And I don't think it makes a lot of sense to invest as much in marketing in the demand environment. Is this volatile and in some cases, weaker. So I think you should think about it as we'll probably put that marketing back in when it makes sense. But in this environment, I think it makes more sense to pull back on that, continue to drive the investment in innovation and the long-term roadmaps.

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah, you said everything I would have said, Nate. I don't think it makes sense to overinvest in marketing when the markets themselves are retracting some employee slot [ph].

A - Nate Olmstead {BIO 21036514 <GO>}

Yeah. And I guess I wouldn't think about that as a signal that we're going to get more promotional as a result of that. I mean, you've heard me talk about having to manage pricing to try to offset some of those pressures. And so I think that remains the focus. In fact, this year, if I look at margins year-over-year, increased promotion was not one of the big drivers of margin pressure. Really, the things that drove margins down year-over-year were currency, cost inflation and logistics rates. Those were the biggest drivers. And so I think we're starting to see some of those things settle down a little bit. The cost increases have definitely slowed. Logistics rates at still at very high levels relative to where they've been historically, but are no longer increasing month-over-month or quarter-over-quarter like they have been. Month-over-month, I would say, they've stopped increasing. So hopefully, we'll see some of those things bottom out. And then as the economy continues to go through this cycle, we can see some favorability and some returns to the costs that we had previously in those areas, which would give us a nice lift on gross margin.

A - Bracken Darrell {BIO 3403495 <GO>}

I'll just add one more thing. I think in my experience, when markets were track like games directing right now, your marketing is just less effective. So I don't think you want to spend as much in and that's what we're doing now. I will come back to September. So we'll come back at it does will probably increase the marketing again. But we still have a lot of marketing spending. We're going to be wrong, even with these numbers, we're still going to be spending a lot of market.

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A - Nate Olmstead {BIO 21036514 <GO>}

Yeah. I think too, Erik, sometimes we talked about the business model and what's the shape of the P&L. And I think these adjustments we're making to the spend are really to help sustain the shape of the P&L. We run OpEx at about 25% of sales. And on this lower revenue outlook and with these OpEx reductions should be seeing us still manage roughly to that same area. You'll see a lower mix of sales and marketing while we continue to sustain investments in R&D.

Q - Erik Woodring {BIO 19492555 <GO>}

If I could just sneak one last one in Bracken, just for you. You mentioned earlier in the prepared remarks a diversification of supply chain outside of China. Can you maybe just elaborate on that a bit what you mean by that? Obviously, you have a big manufacturing base there. But any incremental details would be helpful. And that's it for me. Thanks, guys.

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah, absolutely, Erik. We started -- when we start -- when the tariffs happened a few years ago, I think we had about -- we have less than 1% of our total manufacturing outside of China. So we have -- we had flexibility because really good moving things in and out of our factory, but we really didn't have a supply chain that was set up there. So even though we have the ability to move things in and out, we know the ability to move things in and out very quickly. So we've really been working on that.

The first big wave of work happened during the post tariff kind of right in the middle of the tariff activity. We got to about, I'd say, 15%, 17%. Our goal is to get up closer to 30%, and that will give us flexibility not only in case of other tariffs but also just better cost positions and things. So we feel very good about the progress we're making. We're still very high on China as a manufacturing site, but we want to be flexible. We want to be able to move even beyond that 30% we need to or if we need to, either for costs or for geopolitical area.

Q - Erik Woodring {BIO 19492555 <GO>}

Super. Thanks, guys.

A - Bracken Darrell {BIO 3403495 <GO>}

Thank you, Erik.

A - Nate Melihercik {BIO 20814398 <GO>}

Thanks, Erik. Next up, Adam Angelov from Bank of America.

A - Bracken Darrell {BIO 3403495 <GO>}

Hello, Adam.

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A - Nate Olmstead {BIO 21036514 <GO>}

Hey, Adam.

Q - Adam Angelov {BIO 22341766 <GO>}

Hello. Thanks for letting me on.I think we've gone through most of my questions. So just one from me, please. If the revenue outlook is worse than your guidance, do you think you have further flexibility to call OpEx, if needed?

A - Nate Olmstead {BIO 21036514 <GO>}

There is always opportunity. Like I said, well, I would just say, again, I would think about OpEx, but I would also think about costs overall. It's $4.5 billion if you think about OpEx and cost of goods sold. So again, all that cost is different, but it's a big number. If you're 1% inefficient on $4.5 billion, it's $45 million. So we're not going to wait and find out if the revenue is worse. We're working on all those things today. But it certainly will become tougher. I mean, the more costs you have to take out, it gets a little bit tougher around the edges. But I think that our outlook captures the majority of the outcomes. But if things get worse, we'll make some decisions at that time. We're always going to try to manage our business for the environment, but for the long term. So we want to do things that make sense for the long-term health of the company.

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah, Adam. I'd add to Nate's point. I think -- the way I think about any businesses, you have to adjust to the size of the business. You just have to get some of us. And so we -- it's not a question of can we, we will. The question is how fast are we going to do it, if that happened. But we don't think that's going to happen. But if it did, we'll face into it and deal with it.

Q - Adam Angelov {BIO 22341766 <GO>}

Got it. Great. Thank you.

A - Bracken Darrell {BIO 3403495 <GO>}

Thanks, Adam.

A - Nate Melihercik {BIO 20814398 <GO>}

Thanks, Adam. Our next will be from Ananda, Loop Capital. Good morning, Ananda.

A - Bracken Darrell {BIO 3403495 <GO>}

Hello, Ananda.

Q - Ananda Baruah {BIO 15320341 <GO>}

Good morning, guys. Good morning, guys. Yeah, Nate. Nate, well let me go visual here at either so. So give me a heads up when I can turn it on. But let me just jump into it here, guys. Thanks. Hope you're good. Thanks for taking the question. Yes. So just two, if I could.

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The first is Bracken, you made mention in the prepared remarks or actually, I think it was one of the questions about Asiya's about the segment. Do you expect keyboards and mice to continue to hold up well. Would love to get your thought process behind that. And then I have a follow-up.

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah, I just -- I guess I have several things contributing to that comment and that belief that we have. One of them is that we're also dependent on it today. And I think in a hybrid world, you're going to still be dependent. It's not like the category is going to go away when you go into the office a few days a week, and many of you probably are experiencing that. And I think the awareness is up. And so there's a lot of interest. We're seeing it, and we launch new products. We have much stronger demand than we had before. As we launch a new product, we launched mechanical keyboard to do extremely well. So I think this is -- that's one key dynamic.

The second one is, if you go back to the really heart and soul of this business, it started as a mouse business and then went to mouse and -- mice and keyboard. We have an incredibly good innovation engine in a very, very good strategy for segmentation. And I just feel very good about the vision, the strategy, the execution of the whole thing. So I think we're in more control of our own destiny there than I'd say almost anywhere else we operate. And yeah, so I'm excited about those categories. Like I say that when I came to the company, I actually joined Logitech because all these categories are going to be in a long-term secular decline. They've been a long secular growth trend the whole time and it's getting better and better.

Q - Ananda Baruah {BIO 15320341 <GO>}

Is there --

A - Nate Olmstead {BIO 21036514 <GO>}

Ananda, we actually -- we're tight on supply in some areas of the keyboard and mice market, too. So I think our results there actually could have been a little better if we -- if we had to supply. I mean, that's always the case every quarter. We've got something more short on. And in the recent quarters, it's been there.

Q - Ananda Baruah {BIO 15320341 <GO>}

Do you guys have any sense, look, I know this is mostly a channel sell or what they sell so like not your enterprise sales force. As Bracken, you mentioned a little earlier, but do you have any sense -- any sense, like even if it's super broad, how much goes -- how much of mice and keyboard sales are used for folks in their business environment for a business context? And then secondarily, how much is sort of middle class, upper middle class, so sort of less income sensitive? Well, it's really less inflation sensitive because employment is pretty good. So we don't have an employment issue, we have an inflation issue. So still have discretionary income.

A - Bracken Darrell {BIO 3403495 <GO>}

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Okay. So to answer your first question. Yeah, we have a sense. It's really, as you would guess, it's kind of a hard number to measure, but it's probably about a quarter. And we're underdeveloped in that quarter. We've never done a particularly great job of really attacking the go-to-market through the enterprise of the workspace where you can bet that we're focused there now. So we're going to work to resolve that one.

In terms of kind of high end versus low end or people with a lot of economic availability versus less. I'll just remind you that the average mouse we sell sells for, I think, $29 or $24 in the marketplace. This is not an economic hardship for most people. I mean, it's -- and especially if it's your job or if you're creating them aside, I was talking to a customer today who's actually got two jobs going at once. And this is the lifeblood of your business, doing it well and also just the health and making sure that your hands don't hurt and all that stuff. So I think we're not too sensitive to -- now we're not -- especially the mouse and keyboard, I don't think it's super sensitive to the economic environment. And that's one of the reasons why when we lowered our discussion of where the revenue is going to be, you don't hear us too negative on mice and keyboards. I think even in a recessionary environment, they're going to do okay.

Q - Ananda Baruah {BIO 15320341 <GO>}

That's helpful. And then I'm going to ask one more quick one here. How is the webcam -- I think it's the BRIO's, the high-end webcams that's in the Video Collab segment had those hold up during the quarter? Sorry. What's the -- and how they hold off and also like what's the outlook for them?

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah. Webcam just pulled away back, and I think that's not too shocking. I mean I think people are really scrambling to get on camera. And now most people have found a way to get on camera. So the market pull back. Now it's still way out versus as it was two years ago. So it's a much bigger business today. And we've got -- and we're excited about what kind of innovation we can do there. But I don't want to mislead you. I don't think we're going to turn webcams into a strong growth category in the future. I think it's a good, solid category that's attractive for us. But it's not going to be a heavy focus for us. We're going to innovate there. And I think we'll do well there, and we've got great market share, and we're gaining market share there. But I'm not -- I wouldn't point to that one and say, gosh, that's one to really look at it as a bellwether for how our business is going to do. We know what we think is going to happen there.

Q - Ananda Baruah {BIO 15320341 <GO>}

And Bracken --

A - Nate Olmstead {BIO 21036514 <GO>}

I think about webcam, excuse me, really think about the entire workspace, right? I think rather than -- it's a point of sale, sure, but it's really part of the essential workspace. And so as you're doing more video calls, I think the web camera definitely is more essential than what it was before. So I think that's exciting. The installed base is bigger than it was before because of the sales over the last couple of years. Certainly, it's pulled back off of

those highs. But our strategy is not about that the entire workspace. So it's the web camera. It's the mouse, it's the keyboard, it's the headsets. How do we gain more control, more business of that entire personal workspace and webcam is a part of that.

A - Bracken Darrell {BIO 3403495 <GO>}

Absolutely.

Q - Ananda Baruah {BIO 15320341 <GO>}

And are the webcams that are classified in Video Collaboration, the high-end webcams, were they also softer like your reported segment?

A - Nate Olmstead {BIO 21036514 <GO>}

Yeah, similar to the reported segment, not quite -- not down quite as much, but similar.

Q - Ananda Baruah {BIO 15320341 <GO>}

Thanks, guys.

A - Bracken Darrell {BIO 3403495 <GO>}

Thank you, Ananda.

A - Nate Melihercik {BIO 20814398 <GO>}

And our next question is from Michael Foeth from Vontobel. Hey, Michael.

Q - Michael Foeth

Yes. Hi, thank you for taking my question. Actually, two or three. The first one is on capital allocation and your buyback. The question is actually what are you going to do with all those shares. Are you considering canceling some of them? Or is it all for employee shares? Or do you have other intentions for those shares in order to make them evaluable to shareholders? That will be the first question.

And the second one is really similar or adding up to what you just said on webcams. When you think about the sort of the creator economy and all the devices that these people need, I guess it's mice, keyboard and webcams, headsets. How come there is such a disconnect between mice and keyboards and the other sort of creator economy type of products? And then I have an add-on just on one detail.

A - Bracken Darrell {BIO 3403495 <GO>}

Nate, do you want to take the capital allocation discussion, and then I'll jump on the next one?

A - Nate Olmstead {BIO 21036514 <GO>}

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Sure. Yeah, Michael, there are several uses of them. Some is for employee grants. We could cancel some. We could take some proposals to shareholders at the General Meeting. We don't have anything on the proxy for this year. But we still own a relatively small percentage of that total. So it's not really a decision we face today. But yeah, general uses like we've had in the past, I would say, is the message right now. Bracken, do you want to take the second one or I want to take it?

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A - Bracken Darrell {BIO 3403495 <GO>}

Yeah. No, I think what you're seeing -- what you just described what the opportunity we see is there is a big difference between what people are buying and what they probably need for the creator economy. And as you said, mice and keyboards are growing super well, why are cameras down. We've got one camera that's positioned for that audience. And then we've got a new sub cameras that we've launched called Vivo, which is very, very small. And I think really getting our story. Our marketing story is correct to make sure we're placed in the right places, all those things are really critical to having a long-term really great growth business. It's small today. And the opportunity is really big. I think making sure that a creator feels like they know what they need. We just launched lights, for example. And in a very, very small way, we've launched one light product so far, and it's super interesting to see how many people are looking for that. And we're in very limited distribution so far. So I think there's a big opportunity there, Michael. I think we've just got to keep working to make sure we get the right portfolio, the right positioning for those and the right distribution.

Q - Michael Foeth

Okay. Thank you. And the add-on would be in the audience is the wearables space there. Could you give a bit more detail on what happened in there? What dragged sales done? What went well? And how did the actually -- how did the microphone's business performed?

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah. I would say -- Nate, do you want to cover the overall segment, I'll talk about microphones in particular?

A - Nate Olmstead {BIO 21036514 <GO>}

Sure. Are you including mobile speakers in your question, Michael, or overall?

Q - Michael Foeth

No, no, no. Just the hard and PC wearables.

A - Nate Olmstead {BIO 21036514 <GO>}

Yeah. So I think on the one hand, we had headsets in there, and I mentioned earlier that I think headsets overall was kind of a tough market. So that was probably one of the biggest drivers of the decline. Microphones was also an area that was weaker and Bracken, I'll let you follow up with a comment on that one, but microphones as weaker year-over-year, again, coming off of, I think, a pandemic period where there was probably

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some additional demand for microphones above and beyond the normal creator demand. And then the other pieces of that category are sort of declining as expected. PC speakers, the category, we have very high share, but a market that has been in some decline. And then the last piece I'd probably say would be Jaybird where we've made a decision to not launch new products there. So we're seeing the expected decline in Jaybird as well. Bracken, did you want to comment on mics?

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A - Bracken Darrell {BIO 3403495 <GO>}

Yea. The mics as they said, the mic business grew dramatically during the pandemic. It's still up, I think, more than 50% versus pre-pandemic. And we think a lot of that growth was driven by people just felt like their mic wasn't good enough on their desktop. And so they were not really in that segment you just described is really interesting. They were in another segment, which is the microphone isn't working. And most people have found their way around dealing with that. But the underlying business that of stringers and creators and podcasters, I believe it's still very healthy.

Now in the pandemic, a lot of people got into podcasting that weren't in it performances, probably a big spike and then that's come down. But I think after we get through this period of kind of reduction to the point where you say, okay, this is the real core market, we'll see very strong growth again. I think the need for streaming and creating products is in the world ahead, it's going to be bigger and bigger. And so we're pretty optimistic about it. And we haven't innovated much in our business either and that's coming.

A - Nate Olmstead {BIO 21036514 <GO>}

Still very strategic for us. I think also keep in mind it has some exposure to the Gaming market, which we've talked about has been slower in the last couple of quarters.

Q - Michael Foeth

Okay. Thanks. Very helpful. Thank you.

A - Bracken Darrell {BIO 3403495 <GO>}

Thank you, Michael.

A - Nate Melihercik {BIO 20814398 <GO>}

Okay. Our final question today will come from Serge Rotzer, Credit Suisse.

Q - Serge Rotzer {BIO 4734915 <GO>}

Yes. Hi, good morning, everybody. Yes. Hi, good morning, everybody. I have two quick ones in that case. The first one is, you had a very favorable sales mix in Q1 with Video Collaboration, Keyboards & Combos, Pointing Devices for the high gross profit margin products growing the low gross profit margin product declining. So now we have to expect even not improving margins. but still, we can expect higher volume sequentially, isn't it? Not high single-digit growth, as Nate mentioned, but higher volumes in Q2 than in Q1. Does this imply that the high gross profit margin product -- the high gross profit

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margin product will decline than in Q2. So we see lower sales in Video Collaboration and mice and keyboards or where I'm wrong?

A - Nate Olmstead {BIO 21036514 <GO>}

I think the reality is that the other impacts are just larger than the impact of category mix. We did see favorable category mix year-over-year, Serge. And I saw that in my gross margin bridge. It just wasn't as big as the other ones that I called out. So I think that story still remains. VC, I think, has gone -- it's now over 20% of our mix. It was down about 10% pre-pandemic. So it's doubled in size relative to the overall company. But the other factors are just too big. The cost increases, the logistics rates, the currency, those have kind of overwhelmed most of the other impacts.

Q - Serge Rotzer {BIO 4734915 <GO>}

Okay. Fair point. And the second one is in your inventory, can you remind me how much is finished or finished products and how much is semi-finished products, because these days probably will not ship finished products around the world, given the high cost. You mentioned once you do this only if it gives sense. So I'm wondering in this ratio. And then secondly, obviously, are there any impairment risk then on some of the inventory because it's at the wrong place or you have the wrong products in your inventory at your stock?

A - Nate Olmstead {BIO 21036514 <GO>}

Can you -- I just want to make sure I understand your mix question between sort of raw materials and --

Q - Serge Rotzer {BIO 4734915 <GO>}

The first one is how much is finished products and how much is components, let's say, that way. And then secondly, I fear that on finished products, you could have an impairment risk because you will not ship finished products from Asia to Europe and wherever because it's not worth to do that. So over time, you could have impairment risk on your inventory. What is -- yeah, can you help me there?

A - Nate Olmstead {BIO 21036514 <GO>}

Well, I think on the impairment thing, obviously, that's something we look at every quarter, and we have taken reserves in the P&L really, over the last year, I would say, including some this quarter, we didn't have very many of those during the height of the pandemic growth period because everything was selling. But we've sort of been reverting to more normal levels of reserves, I think, over the last 12 months. So that continues and something that obviously gets very close inspection every quarter to make sure that things that are aging or slow moving or things to come back from customers, those all carry reserves and that's all reflected in the P&L.

The other thing to keep in mind, too, Serge is, our business mix has shifted. So we started off your question talking about VC. It's a very different category than, say, music speakers, right, which was -- which is a category we deemphasized, it's now just a couple of points of our sales. So that was a category and Bracken mentioned why sort of the

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unattractiveness of that business model. It was a much more discretionary purchase, had much higher holiday sales, VC is a much steadier demand product, longer life cycles and so forth. So I think the overall amount of risk in the types of inventory that we're holding is different than what it was a few years ago as our business has shifted to more mice and keyboards, which have long product life cycles, more VC, which have long product life cycles, things like that.

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A - Bracken Darrell {BIO 3403495 <GO>}

Yeah. I would just add to that. I think we're also just -- I mean you know this because you've been following us for a while, but I'll say for everybody else. We're not in a business that has big obsolescence risk, where new technology is going to come in really obsolete our category. I mean if we have a risk, it's -- we have a little too much inventory in one place or another one, and we need to just be patient and get it out, not hyper discounted to get it out. And that's generally the approach we've taken. I'm not saying we don't have any inventory risk you always do, but it's not -- it doesn't look like many of the categories that you probably look outside of us.

Q - Serge Rotzer {BIO 4734915 <GO>}

Okay. Got it. Many thanks and congratulations. Bye-bye.

A - Nate Melihercik {BIO 20814398 <GO>}

Thanks, Serge. Thanks, everyone, for your questions. Bracken and Nate, thank you. That's a wrap on our call, Bracken, any final comments.

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A - Bracken Darrell {BIO 3403495 <GO>}

No, I really appreciate it. It was a great high engaged discussion today. Thank you very much. We look forward to talking to you again next quarter, and stay tuned. It's an exciting time in the world. Every first quarter of the year seems to be very different from the last one over the last three or four years, and we're in another one now. So -- but I'm very optimistic about the future. I think we're in a great spot.

A - Nate Melihercik {BIO 20814398 <GO>}

Wonderful. Thanks, everyone.

A - Bracken Darrell {BIO 3403495 <GO>}

Thanks, Nate.

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