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Q3 2023 Earnings Call

Company Participants

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

Other Participants

- Adam Angelov, Analyst
- Andreas Mueller, Analyst
- Asiya Merchant, Analyst
- Erik Woodring, Analyst
- George Wang, Analyst
- George-Samuel Brown, Analyst
- Joern Iffert, Analyst
- Michael Foeth, Analyst
- Paul Chung, Analyst

Presentation

Nate Melihercik {BIO 20814398 <GO>}

Okay. Good morning and good afternoon, everyone. Welcome to Logitech's Video Call to discuss our Financial Results for the Third 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 Reform Act of 1995. We're making these statements based on our views only as of today. 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 and forward-looking statements 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 will all be available at the Investor Relations page of our website. We encourage you to review these materials carefully and unless otherwise noted comparisons between periods are year-over-year and in constant currency and sales or net sales. And finally, this call is being recorded and will be available for replay on our website.

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

Bracken Darrell {BIO 3403495 <GO>}

Good morning, Nate. And thanks Nate and thanks all of you for joining us. As you saw in our pre-announcement, our third quarter results were disappointing. Enterprise demand deteriorated versus last quarter and consumable purchases were soft and more concentrated during promotional weeks than it's typical. Those factors pressured our net sales and gross margins and resulted in a revised fiscal year '23 outlook.

I discussed for the past few quarters the ongoing macroeconomic and geopolitical challenges impacting Logitech and the world. A strong dollar, global inflation and low consumer confidence continue. In the midst of these, we focus on what we can control, product innovation, a strong go-to-market strategy and disciplined P&L management. So what changed during Q3 that pressured our results? First, our enterprise demand declined. Our VC -- our VC business had delivered consecutive quarters of 7% growth and fell 16% this quarter. You all have read the headlines Google, Amazon, Microsoft, banks and other businesses have announced layoffs and cost containment actions. Initially resilient in the face of pressured macro conditions, businesses are increasingly cautious in their spending given the economic volatility and uncertainty and, of course, that is impacting our enterprise business too.

The second change in this quarter was a shift in our consumers purchasing patterns. Consumer sales remained weak and importantly, of those consumers that did buy these purchases were concentrated in times of higher promotional intensity resulting in lower sales and pressured margins. While current macroeconomic conditions and even the variables that changed the third quarter aren't going away this quarter, they don't impact our view of the long-term potential of this business. We remain committed to the long-term growth trends, strong market strategy, the markets and the business models we have in place. Over time, I fully expect this to return to more predictable, less volatile economic conditions and I believe this does support business investment, rising consumer confidence, sustained growth at Logitech because if we -- if we look beyond the whipsaw of the daily headlines, I'm actually struck by what hasn't changed. While the pace of return to office remains uneven, hybrid work is inevitable. Companies approach to return to the office has been different across the industries and geographies. I hear a familiar story from CEOs and customers across industries. They're still working to determine what hybrid model works best for their teams. Logitech is no different. We're relocating and redesigning buildings in the Bay Area and across the globe, focused on a hybrid work environment. As companies settle out on their definitions of hybrid work, we should see investment in personal workspaces and collaboration rooms. This investment will happen. It's just a question of timing.

Product innovation matters more than ever. The winners will have great products. That's why we keep investing. We're also diversifying the ASPs in our portfolio through innovation across all categories. Our oldest business, Pointing Devices had ASPs 25% higher this quarter than four years ago as we've systematically expanded the category into new segments with differentiated features. This is obviously by design, making sure we have category defining products across a broad range of ASPs base fees is our goal. Innovation

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requires investment in R&D investment, this quarter was up 50%, more than we invested in Q3 2020. Few companies have the financial resources and the management discipline to sustain investment in product development during challenging times, while driving efficiency at the same time. We continue to press that advantage and are enhancing our product portfolio. The big durable trends we've been highlighting, video everywhere, hybrid work, the explosion of gaming and content creation, continue to move ahead. People today want to work, play and create from anywhere. And we believe that our products will be a great enabler of this trend.

Let me provide a little more perspective on this quarter's performance. I mentioned consumer spending was weak in the quarter and it was. With sell through, excluding currency and our prior business in Russia and Ukraine, all declined mid-single-digits. We grew market share in Gaming, Video Collaboration, Pointing Devices and Tablet Keyboards.

In Video Collaboration, while the number of conference cam units declined year-over-year, we continue to drive ASPs per room higher. The mix of our conference room sales skewed toward the securing the high-end cameras and attach rate of accessories and services to our conference room camp sales is growing, which drives our sales revenue per room, higher. We evidenced that our strategy developing integrated room systems is working.

In keyboards and mice, we continue to gain share in the fast-growing high end of the market. So what can you expect from us in the near-term? You should expect us to operate in a conservative disciplined manner consistent with the last few quarters, namely real focus on decreasing our expenses. We plan to reduce operating expenses by $150 million, or 11% by the end of fiscal year '23. We're on track to well exceed that goal. For Q3, OpEx was down 23%. You've watched us be aggressive on our OpEx as we saw the market weaken, and you can expect us to continue to manage our costs based on market conditions.

We'll continue to invest in product development though. Customer needs are evolving quickly. We have the engineering and design expertise, customer insights and financial flexibility to bring new products to market to meet this demand and to accelerate refresh cycles. And we will lean into our global operations and go-to-market capabilities.

One final note before I hand it over to Nate. First, regarding our CFO search, our search is progressing well, but we don't have an update currently to share with you today. Second, I'm really pleased to announce our current Head of Global Operations and Sustainability, Prakash Arunkundrum, has been appointed Chief Operating Officer here at Logitech. Prakash has been here for close to seven years and is a frequent presenter at our Annual Analyst and Investor Day, so many of you already know him. In this newly created role, Prakash will be one of my key partners in making sure structured strategically and operationally for the short- and long-term road ahead.

With that, I'll hand it to Nate to provide some additional color on our results. Thanks, Nate.

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Nate Olmstead {BIO 21036514 <GO>}

Thanks Bracken. Hello, everyone. Let me walk you through the quarter in more detail. Our Q3 results were impacted by a challenging macro environment. Net sales were down 17% to $1.27 billion. This reflects consumer purchasing concentrated in promotional weeks throughout the quarter and lower enterprise and consumer spending. Gross margins decreased versus last year to 37.9%. Versus the prior year, currency was unfavorable three points, promotions were also unfavorable three points and cost inflation was unfavorable two points. These eight points of headwinds were partially offset through our pricing actions and by driving down our use of expedited shipping.

Operating profit was $204 million, reflecting lower demand and gross margin pressure, partially offset by reductions in operating expense. Cash flow from operations was $280 million in Q3 and cash flow was up $118 million year-to-date versus last year.

Turning to results across our product categories. Gaming was down 10%. Growth in our simulation products was essentially flat and more than offset by declines in PC and Console Gaming. Asia Pacific was down only modestly while Americas and Europe remain pressured. Despite these declines, we gained market share in nearly all gaming categories.

The largest negative swing in our portfolio versus last quarter was in Video Collaboration, which was down 16% after posting consecutive quarters of 7% growth. Video Conference Room Cameras and Peripherals declined single digits, but we gained share. And business-oriented webcams were down more than 40%.

Pointing Devices were down 8%, driven by pressure in the low end of our portfolio, but we grew market share in total Pointing Devices. Keyboards and combos net sales declined 17% with gains in the high-end of the market, offset by losses in the low-end of the market. And consumer webcams were down nearly 50% year-over-year.

Turning to expenses. Consistent with last quarter, we reduced our OpEx, which was down 23% versus last year. As Bracken mentioned earlier, we remain committed to investing in product design and development to strengthen our category leadership. And while R&D was down modestly versus last year, the $63 million we invested in R&D in Q3 is more than 50% higher than our R&D investment level just three years ago.

In Q1 of this fiscal year, we communicated our plan to reduce our annual operating expenses by $150 million versus last year. And we achieved that goal this quarter, one quarter ahead of schedule. I now expect that for the full year, we will reduce operating expenses by approximately $215 million or 15% versus last year. We will continue to focus on finding efficiencies throughout the organization as we manage our costs based on market conditions. We ended the quarter with a cash balance of more than $1 billion and continued a strong share buyback program returning $90 million to shareholders in the quarter.

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We revised our financial outlook for FY '23 based on three items; softer than expected third quarter results, enterprise and consumer demand, which may remain weaker than we previously expected, and uncertainty and supply availability related to the recent COVID outbreaks in China. Our outlook calls for full year revenue in FY '23 to be down 13% to 15% in constant currency. The US dollar weakened versus last quarter, but currency still projects to be roughly five point headwind to US dollar growth for the full year. Therefore, our outlook for full year revenue in US dollars would be down 18% to 20%. Our full-year non-GAAP operating income and outlook is now between $550 million and $600 million.

Nate, we can now open the line for questions.

Questions And Answers

A - Nate Melihercik {BIO 20814398 <GO>}

Great. Thanks, Bracken. Thanks, Nate. As a reminder for those on the call, please raise your virtual hand and we'll get you in queue for Q&A with Nate and Bracken.

Our first question is from George Brown at Deutsche Bank. Good morning, good afternoon, George.

A - Bracken Darrell {BIO 3403495 <GO>}

Hi, George.

Q - George-Samuel Brown {BIO 22577500 <GO>}

Good afternoon. Thanks for taking my questions. I have two if I may.

A - Bracken Darrell {BIO 3403495 <GO>}

Okay.

Q - George-Samuel Brown {BIO 22577500 <GO>}

Firstly, in terms of product launches, you released quite a few products, in Q2, ahead of the holiday season. Can you provide some detail on how they performed? And in particular, I'm interested in how Logitech G-Cloud has performed, and I wonder met your expectations or not? And I'll leave it at that.

A - Bracken Darrell {BIO 3403495 <GO>}

Okay. Yes, I would say, overall, we announced 20 new products that we're launching in Q3 or sometime in the next six to three to four months after that. And I would say overall our launches are pretty well on track. The G-Cloud, in particular, is a very narrow launch. So we launched it already in the US. We are so far so good. We're now expanding into Europe and Japan. So I would say so far it's on track. It's a new category for us. We're always very conservative on new categories, George, because we don't want to get over the tips of our skis as we'd say here, but so far so good. And generally speaking, I feel really good

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about our innovation in total. I mean we continue to have just a really, really good insight-driven innovation with. And I would say, our performance in all of our new products is pretty well on track.

Q - George-Samuel Brown {BIO 22577500 <GO>}

Perfect. And then just a second question. And just in terms of the level of discounting going forward and also that was clearly some pull forward demand during the Black Friday and Cyber Monday period. And what can we expect in going forward into Q4, and beyond from a promotional perspective, given inventory signs at quite high level?

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah. I don't think we're not -- we're not in a position right -- so we're going to heavily discount because of the inventory levels. Our channel looks fine, and our internal inventories came down quarter-over-quarter, again, as you probably saw. But we're going to make sure we're responsive to the environment. So I wouldn't commit to you exactly where the overall promotional levels would be. I think they were particularly high as a percentage of our business this quarter though, and I wouldn't expect that again.

A - Nate Olmstead {BIO 21036514 <GO>}

Yeah, George. Just two quick comments on your questions. First, I think from an NPI standpoint, agree with Bracken, off to a good start. I wouldn't say there was anything in there that was financially really that significant in the quarter, so still ramping up there. And then on the discounting, as Bracken said, we definitely saw consumer preference towards more promoted products this quarter. I think there some of that assumed going forward here in Q4, too early to say what that looks like out into next year, I would say, but that seems to be the environment that we saw during the holiday were certainly the weeks with the higher promotions had the higher percentage of sales.

Q - George-Samuel Brown {BIO 22577500 <GO>}

All right. Thanks guys.

A - Bracken Darrell {BIO 3403495 <GO>}

Good.

A - Nate Melihercik {BIO 20814398 <GO>}

Thanks, George. Next up from Asiya Merchant from Citi. Good to see you Asiya.

A - Bracken Darrell {BIO 3403495 <GO>}

Hey, Asiya.

A - Nate Olmstead {BIO 21036514 <GO>}

Hey, Asiya.

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Q - Asiya Merchant {BIO 20247269 <GO>}

Hey. Hey, good to see you guys too. Couple of questions. First on the VC side of things. Where -- if you can give us any anecdotes about how your discussions with customers are going now, clearly the environment is still pretty gloomy out there as far as layoffs. But has there been any change since their reported quarter in terms of these conversations with these customers around demand for BC. And then secondly, I know in the press release and Nate mentioned that as well, there are some supply concerns for your March quarter that you discussed in the press release with the pre-announcement. Can you tell us how much of that's really affecting the March quarter? And when do you expect those to kind of play out? Or are you still expecting supply issues post the March quarter? Thank you.

A - Bracken Darrell {BIO 3403495 <GO>}

Okay. I'll take the first one, Nate, I'll let you take second one. I'd say overall -- I just came back and see some -- yeah, I would say generally speaking the term was about the same, everybody seems very committed to the long-term, making sure they've got the right setups and that -- I wouldn't say there's any real change in the secular term from what I see. But, I do feel -- I do sense the conservatism. I think you could hear it and some of our sales people are saying March, March, March. And I'm not sure that was the right date, but they're saying a lot of the companies really pushing out spending into future quarters. So I think that's probably still out there. And we're certainly assuming that as we go into Q4 and its reflected in our guidance. Nate, do you want to take and try the question.

A - Nate Olmstead {BIO 21036514 <GO>}

I'm happy to. Yeah, no, I think -- listen, I think the thing that we probably all learned over the last few years with COVID is it's a little hard to predict. So I've made some assumptions that there could be some disruptions on supply in the quarter. We're working hard on those things. We may have opportunities through expedited freight and so forth to recover some of that, but still a fluid situation Asiya. So there's not really a specific number I would say. We called out -- just tried to factor in a range of possibilities in the outlook. And so that was one of the things that caused us to adjust the full-year outlook.

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah. I would just add to that. I think we're in that -- we're probably in the middle of the most uncertain period right now, because it's -- you're just starting. All of our factory people are back to their homes. And it's anybody's guess on what that's going to do with COVID rates and whether we will have problems getting people back or some of our suppliers. So, we're in this kind of uncertain period now. But -- but I think it'll settle out over the next few. It's not an unlimited risk, so we bracketed it pretty well, I think in our outlook.

A - Nate Olmstead {BIO 21036514 <GO>}

I think the other thing that we've done that certainly over the last couple of years through investment has been increasing out of automation in the factories, so we can fully offset the risk of labor disruptions and things like that, but we have improved the company's ability to do that versus couple of years ago by driving up that automation in the factory, which is somewhat reduced the reliance on labor, but still something that we've got to really manage tightly.

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Q - Asiya Merchant {BIO 20247269 <GO>}

Great. And then just in terms of growth outlooks beyond the March quarter. You guys, obviously, have the target model out there. Any indication on when we should expect that growth? Are we at a point where post-March quarter? We can return to kind of the growth rates that you guys have outlined just given the macro trends that you're so confident on will continue?

A - Bracken Darrell {BIO 3403495 <GO>}

Well, certainly, we're planning Analyst Investor Day. We'll have the data out there shortly. I think it's too early for us to tell you what next year is going to look like. And -- but hopefully we'll have a clearer picture of that when we come into March. I don't think -- I can't imagine that we're going to see a snapback in the macroeconomic picture in a quarter. So I wouldn't expect it to -- our fiscal year end and then things suddenly get better. But I think I'm pretty optimistic about somewhere out there in the next -- over the next year or so that you'll see the market come back where I think everybody on this call has an opinion on how long this is going to last.

Q - Asiya Merchant {BIO 20247269 <GO>}

Okay. Thank you.

A - Bracken Darrell {BIO 3403495 <GO>}

Thank you.

A - Nate Olmstead {BIO 21036514 <GO>}

Thank you, Asiya.

A - Nate Melihercik {BIO 20814398 <GO>}

Great. Next up will be Paul Chung from JPMorgan.

A - Bracken Darrell {BIO 3403495 <GO>}

Good morning, Paul.

A - Nate Olmstead {BIO 21036514 <GO>}

Hey, Paul.

Q - Paul Chung {BIO 21446425 <GO>}

Thanks for taking my questions. So just on gross margins, as we kind of think about couple of quarters down the line, how do we think about pricing increases? You've done kind of lapping some FX headwinds, lapping some component inflation and lower shipping costs. Can we rebound comfortably into your kind of target of 39% to 44% in a couple of quarters?

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A - Nate Olmstead {BIO 21036514 <GO>}

I go and take that one Bracken. Yeah, I mean, Paul, this quarter we had eight points of headwinds year-over-year for similar factors in a sense that we had currency was the largest. We also did have some headwind this quarter from the increased promotional mix and then we also had the inflation. As I mentioned last quarter, I mean I think we feel good about some of the trends on the inflation side start to see some of the cost come down, ocean freight, we continue to make some progress on the rates there. And currency looks a little bit more favorable than it did last quarter. So good trends, but we didn't really see any of that really flow through yet this quarter. And I think next quarter, I really don't expect to see a lot of that favorability yet. It takes a little bit of time with the inventory, be in a little bit higher, we've got to work that down to start seeing some of those benefits come through as well. But yeah, I think into next year, I think some of these tailwinds could probably become -- excuse me, some of these headwinds could probably become tailwinds. I think I misspoke earlier those were obviously headwinds. Some of those headwinds could become tailwinds. And I think in terms of the pricing -- I think it's good that we took action early this year to increase prices across a number of categories. That's helped offset some of these pressures. And we see what the promo environment and what kind of promo environment unfolds over the next few quarters, whether we can hold those or not. So, lots of moving pieces, Paul, but I do think that we've been absorbing a lot of those headwinds this year and I do expect some of those begin to reverse into next year.

A - Bracken Darrell {BIO 3403495 <GO>}

And maybe Paul, one more from price perspective. I think the thing that makes me feel the best about this year is the incredible amount of headwind we're facing from a gross margin standpoint. Exactly when that reverses is a little unclear. I mean, clearly currency is on its way now. We're not seeing it yet, but -- it's carbon hedges and natural hedges and technical hedges, et cetera, but I'm super excited that we have 800 basis points of headwind, because that's going to come back out again. But we're not going to see 800 basis points of improvement, but getting into that range again, I'd sure hope we do it next year.

Q - Paul Chung {BIO 21446425 <GO>}

So by next year, you mean next fiscal year or so. So when are you planning, 2Q or --

A - Bracken Darrell {BIO 3403495 <GO>}

Yes, that's true.

Q - Paul Chung {BIO 21446425 <GO>}

Okay. And then just a follow up on OpEx, pretty material cuts. What do you kind of see normalizing assuming more aggressive cuts maybe in the near term? Do we get back to that 25% of sales? Or where are you seeing further opportunities to kind of right size costs, while top line challenge? Thank you.

A - Nate Olmstead {BIO 21036514 <GO>}

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(Multiple Speakers) Paul, I think on a full year basis, you probably see the OpEx be around 25%, which is where it hasn't been. And come back to your earlier comment on gross margin, those things go hand-in-hand. So if we get good confidence in line of sight of gross margin expansion, that creates more room for investment if we see good returns available to us to drive growth. So that strategy remains unchanged moving away from a promotion-driven strategy to one that's more pull-driven through increased marketing investments. Certainly, we're committed to the investment in product innovation and we think that's key. Bracken, something you'd like to add to that?

A - Bracken Darrell {BIO 3403495 <GO>}

No. You got everything. Perfect.

Q - Paul Chung {BIO 21446425 <GO>}

Well, thank you.

A - Bracken Darrell {BIO 3403495 <GO>}

Thanks, Paul.

A - Nate Melihercik {BIO 20814398 <GO>}

Thanks, Paul. Next up from Morgan Stanley, Erik Woodring. Good morning, Erik.

Q - Erik Woodring {BIO 19492555 <GO>}

Hey, guys. Good morning. Thank you for taking my questions. I guess maybe first, if we take a step back and think about kind of your four major end markets. Where do you think some of those are furthest along in terms of kind of facing the brunt of the challenges the world faces today, meaning we saw PCs correct earlier perhaps and consumer electronics, which perhaps has corrected earlier than enterprise. And so just curious where you think, you could perhaps see maybe a rebound first relative to other of your end markets? And then I have a follow-up.

A - Bracken Darrell {BIO 3403495 <GO>}

Well that is really a good question. I'm going to hesitate to give you a definitive answer, but I'll give you kind of a feel. I think it could be that we see it first in game, but it kind of depends because the gaming market has also seems pretty sensitive to promotion this quarter. So that maybe a little less -- it makes me a little more tentative to say that. I think the enterprise spending kind of comes in later and starts -- starts out later and it hangs longer and then comes out little later when you go into a soft -- softening of the economy that's generally the view. And then our personal workspace business that's somewhere in between. I reserve the right to completely reverse though. To be honest, the visibility is not what we'd like. It's really hard for us to see. But I think, the good news on all three is I really feel good about the long term, I do think those secular trends are super solid.

Q - Erik Woodring {BIO 19492555 <GO>}

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Okay. No. That's helpful. And then just because you mentioned it Bracken, I'd love to just maybe get some color from you guys on maybe why visibility is different than historically? Is it different purchasing patterns? I know you mentioned the purchasing during promotional have heavy periods in the December quarter. But maybe just taking a step back, our enterprises purchasing at a different cadence than they used to, our consumer preferences for purchasing changing, I would just love some more color on just maybe how that visibility has changed? And or when it could improve and why it might improve? Thank you so much.

A - Bracken Darrell {BIO 3403495 <GO>}

Sure. Absolutely. Thanks, Erik. I just flew them in those two pieces. On the consumer side, I think you said that you said it all the consumer demand has been weaker, and in this quarter we saw really concentrated in promotion. Now, I hope that Nate -- we're saying, we're assuming it could be more promotional as we go through the rest of the year, I hope that it start -- that starts to fade at some point soon because -- normally promotion is heaviest during a holiday quarter. Now, we may see that in Q4, but we'll see -- but we're prepared for that. But I hope that it will start to get better from a promotional standpoint. And that is not -- that would not be normal to have heavy promotion go on all the way through outside of the holiday quarter all the way through the year. So we'll see. On the B2B side, it really -- just comes down to, I think, there's such turmoil that maybe too strong in term, but there's a lot of settling that's happening. I can't remember since I've been in this job anyway, when we've had the kind of layoff announcements that we've had over -- just the last 90 days. I think there's just a lot of constriction of spending happening. And I think that automatically drops your visibility. What you think you have in visibility suddenly gets pushed. It seems like we pushed out a quarter two or something. So I think that's the mistake. I think, I like the fact that it's actually sharp production right now from a business standpoint, because I think that means that might be a faster exit back out again. But maybe that's my optimism poking it set up, but I would rather see that than see people kind of gradually easing into something. So I'm sort of feeling good that there's all this discussion around construction. And I feel good about our business, they aren't going to be wrong. But I feel good about the restriction, I think that suggested people are making the right steps and then the clarity will come, as we go into next year.

A - Nate Olmstead {BIO 21036514 <GO>}

And if I could add just a little bit to that Erik, as I think --

Q - Erik Woodring {BIO 19492555 <GO>}

Yeah. Please, of course.

A - Nate Olmstead {BIO 21036514 <GO>}

You asked what causes it to be different. I think we're transitioning out, obviously, a unique period globally from shutdowns. And so the diversification that we have, again, I'll come back to this in the portfolio by product, by category, by geography, are all things that I love having in a time like this because that transition is, obviously, different in those categories and in those geographies. You can still see, places that are doing better, that are growing a little bit, they maybe went into that lockdown at a different time, they've come out of it

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differently. So that diversification continues to be, I think, really, really important thing. Obviously, this quarter we're disappointed with volumes. But the shape of the P&L held up pretty well. And I think we continue to manage well in this environment. We continue to do well from a market share standpoint. We continue to invest in our long-term priorities and continue to manage OpEx, I think, very well, and do a good job of cash generation. So lots of things haven't changed. And again, I think the diversification in our business is really key that has been able to deliver a good strong quarter and was a challenging macro environment.

Q - Erik Woodring {BIO 19492555 <GO>}

Okay. That's super helpful. I was just -- the last and very quick follow-up was, when you mentioned enterprise demand weakens, what -- did it spillover into any other segments besides VC or was it mostly concentrated in VC? Just want to share that clarification. That's it for me.

A - Nate Olmstead {BIO 21036514 <GO>}

We see it also in C&P, and mice and keyboards -- mice and keyboards and traditional mice and keyboards and Video Collaboration are two biggest areas in B2B. VC is a good proxy for us, because it's pretty much all B2B, but we also see it in mice and keyboards.

Q - Erik Woodring {BIO 19492555 <GO>}

Okay. Thank you.

A - Bracken Darrell {BIO 3403495 <GO>}

By the way, I should say, it's not like people are buying any conference cams they were. So we didn't suddenly go terribly negative where it's down mid-single digits. So, but that was after bring up double digits before.

A - Nate Olmstead {BIO 21036514 <GO>}

Right.

Q - Erik Woodring {BIO 19492555 <GO>}

Thank you guys.

A - Bracken Darrell {BIO 3403495 <GO>}

Thank you, Erik.

A - Nate Melihercik {BIO 20814398 <GO>}

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

A - Nate Olmstead {BIO 21036514 <GO>}

Hey, Adam.

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Q - Adam Angelov {BIO 22341766 <GO>}

Hi, there. So just wanted to check on the channel inventory situation. So maybe if you could go by division. So I think Gaming was positive sell-through in the quarter. Is that a sign that the inventory levels there are kind of at reasonable levels, and perhaps the sell-in can match the sell-through going forward? And maybe if there is any other specifics by different division, if you could add that, that will be great. And then second one, so on 2023, the calendar year, are you thinking about further price increases? And maybe if you could just share your thought process on price increases versus potentially prolonged promotion periods as we -- as you mentioned already? Thanks.

A - Bracken Darrell {BIO 3403495 <GO>}

Nate, I'll let you take the first one, and I'll take the second.

A - Nate Olmstead {BIO 21036514 <GO>}

Yeah. I think channel is in good shape. It's down year-over-year, which would be consistent with the overall trends in the business. I mean, I think, we continue to see our customers, I think being pretty cautious and conservative around restocking. Same sorts of visibility challenges that we were talking about a moment ago, I think probably apply to them as well. So, being a little cautious on reordering. But the channel's in good shape. As Bracken mentioned, gaming was one of those areas that was more -- seemed to be more promotional this holiday period. And so we did make some progress in reducing some of the inventory levels there. I'll just quickly say on the pricing side and then I'll let you jump in there too Bracken. It's really a function of a lot of things Adam. What happens with currency? What happens with inflation? So lots of elements of there for us to consider. But Bracken something you'd want to add on that?

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A - Bracken Darrell {BIO 3403495 <GO>}

I'll be more definitive. I mean if something doesn't change, I can't imagine us raising price further. I think those 900 basis points or 800 basis points of headwinds are -- that are going to eventually drop, which suggests that we won't need to -- if something radically changed again, who knows, but I don't think as long as currency keep setting in the direction there is some inflation keeps heading in the direction we all think it's going to go. I don't think we would need to raise price again.

A - Nate Olmstead {BIO 21036514 <GO>}

And then on the inventory side, so you asked about channel, again Bracken had mentioned, I think in his remarks. Third consecutive quarter where we've reduced our distribution center inventory sequentially. And we made good progress, I think there in this quarter. We'll be able to reduce that more into the fourth quarter and continue to normalize those levels. Not in a big hurry to do so. It's all good fresh inventory that I expect we'll sell, but continues to be a focus for us.

Q - Adam Angelov {BIO 22341766 <GO>}

Right. Thank you.

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A - Nate Olmstead {BIO 21036514 <GO>}

Thanks Adam.

A - Nate Melihercik {BIO 20814398 <GO>}

Next on the line will be Joern from UBS. Good afternoon, Joern.

A - Bracken Darrell {BIO 3403495 <GO>}

Hey, Joern.

Q - Joern Iffert {BIO 15374623 <GO>}

Yes. Hi. Good morning. Thanks for taking my questions. And the first would be please, on your implied Q4 outlook, which is targeting guiding for sales being down around 25%. Can you really get us a rough indication is one third of this fees staffing, one third consumer demand weakness and one third China, is this how we should think about it, because it seems when you're saying it looks like through for your key categories ex-Russia was only down mid-single-digit in Q3? It seems a quite sharp deceleration. So if you can provide some more color here. Would be definitely appreciate it. And the second question would be please, just focusing on the freight cost, which they came down to pre-COVID levels for a couple of areas. And do you see that this will be a very strong contributor -- see those variables to your earnings growth in 2024? And maybe to start with these two questions. Thanks.

A - Nate Olmstead {BIO 21036514 <GO>}

I'll take the first one. Yeah. And then I can get the second one too. In the outlook for Q4, really implies typical seasonality Joern, from Q3 to Q4. So Q3 was weaker than expected. And off of that, you would get sort of a normal mid-20% decline sequentially into Q4. So that's what -- so with the guidance really implies. We've got one quarter left, but the full year guidance basically implies that for the fourth quarter. And then on the freight cost, the benefit we got this quarter was that we didn't use air freight to the same level by long ways versus last year. We were chasing a lot of supply last year, it's not the case this year. So we were able to reduce our air freight. So we got some year-over-year benefit there. We're still -- and ocean rates are getting -- are coming down, but they're still higher than what they were pre-pandemic. So it come down month-on-month, starting to look more positive there, but still have ways to go before we get back to pre-pandemic levels.

Q - Joern Iffert {BIO 15374623 <GO>}

Okay. And then maybe the last question, if I may, on your OpEx. When we look in 2024, I mean, after you take out $250 million OpEx in fiscal year '23, is this now enough? Is this done? Are you living enough, for example to call with flattish 2024? Let's say for you good about, let's say more to come now in the next couple of quarters regarding your plans?

A - Nate Olmstead {BIO 21036514 <GO>}

Yeah, I want to clarify a real Bracken. I'm not sure if we said 250, but I said 215, 1-5.

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Q - Joern Iffert {BIO 15374623 <GO>}

15. Yeah, yeah. Okay. Thanks.

A - Nate Olmstead {BIO 21036514 <GO>}

I wanted to make sure that you heard that clearly. Bracken, sorry, did you have a comment.

A - Bracken Darrell {BIO 3403495 <GO>}

Yes. And I'll just -- yeah, 215. And we're going to keep -- we're going to keep up the OpEx. We're not letting up. When we look at the top line, we feel like we need to take -- we're going to continue to take more. And so you can count on that. We'll keep aggressively taking out. We're going to respond to market conditions and you see what they are. So you can imagine how we feel about our costs.

Q - Joern Iffert {BIO 15374623 <GO>}

Okay. Thank you.

A - Nate Olmstead {BIO 21036514 <GO>}

Thanks, Joern.

A - Nate Melihercik {BIO 20814398 <GO>}

Our next question is from Andreas Mueller at ZKB.

Q - Andreas Mueller {BIO 16350975 <GO>}

Yes. Hi everybody. Hope you're well. I have two questions. One is really, can you say something about the Chinese sales in the quarter? And do you expect that the impact from the leave restrictions going forward? Is that the benefit or not? And then property also this status, I mean, you mentioned something in your production facility. Are you completely 100% operational right now? And what is -- what's there to status basically?

A - Bracken Darrell {BIO 3403495 <GO>}

I'll answer the second one. You take the first one, Chinese sales.

A - Nate Olmstead {BIO 21036514 <GO>}

Yeah, on Chinese sales, I mean, China unfortunately was negatively impacted this quarter from a sales standpoint due to the infections, the rise in infections. I think we probably had about one point headwind this quarter, Andreas, from sales in December that didn't occur, I think longer term, I mean, I think it's a positive, it's potentially a positive. But like I mentioned earlier, I mean, I think COVID is just unpredictable. And hopefully this was sort of a one-time event, but I think that's not for me to know with certainty. So, but I think it's a positive to see a more open position by the government, I do. But we do have in this quarter.

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A - Bracken Darrell {BIO 3403495 <GO>}

I'll add to that. I do think. I think opening -- China opening is positive. And I think -- you asked about our production facility related to that. Right now our production is still exposed because of Lunar New Year. So that's one of the things that has given -- that gave us little pause with what happens during Lunar New Year and thereby (inaudible) come back. And I'd say, we'll see, I mean, I think we'll manage whatever it is. But that is what it is. But I'm actually -- I hear so many negative headlines about China. I feel like the -- the optimist in the room on that for sure. I feel good about China. I think as China opened, it's going to be good for us. It's our second biggest market. It's always been a good market. As long as I've been here, it's been good. We've had very few times -- we had a long period of slow growth there. So I'm excited about China. We've got a great market share. We've got a great brand there. And we're really learning a lot about the Chinese consumer there. So, yeah, I'm optimistic.

A - Nate Olmstead {BIO 21036514 <GO>}

Thanks Andreas.

Q - Andreas Mueller {BIO 16350975 <GO>}

Okay. Then is another question about your priorities. When you go through your portfolio, do you see any need for changing some priorities, for some categories with the downturn, maybe to earmark also a category as non-strategic one more besides say mobile speaker and the earbuds, for example?

A - Bracken Darrell {BIO 3403495 <GO>}

Yeah. We've kind of done that and we always will do it. And we do it on a very regular basis, so as you mentioned here, we picked out a couple of categories that we said we are non-strategic, which means we're reducing our investment and we stayed true to that. I don't see any immediate changes in our current. Last time we updated you, but we'll -- we'll update you again at the Analyst and Investor Day. I think our portfolio -- I'm really excited about that kind of 80% of our portfolio that we've angled for put our investment into. We're gaining market share across those. We're investing aggressively from an engineering standpoint into them. And, yet, we're managing costs really well across the Company in the middle of this -- in this current economic storm. And so I think that bodes well for the future. But, we'll update you again regularly. We'll keep you updated on where we are deemphasizing categories.

Q - Andreas Mueller {BIO 16350975 <GO>}

Okay. Thank you very much.

A - Bracken Darrell {BIO 3403495 <GO>}

Thanks, Andreas.

A - Nate Olmstead {BIO 21036514 <GO>}

Thanks.

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A - Nate Melihercik {BIO 20814398 <GO>}

Our next question is from George Wang at Barclays. Hey, George.

A - Bracken Darrell {BIO 3403495 <GO>}

Hey, George.

Q - George Wang {BIO 17439572 <GO>}

Hey, Bracken. Your first question is, maybe you can give more color just in terms of the latest B2B consolidation in terms of the go-to-market kind of sales force? And how you guys are applying learnings from the consumer vertical kind of innovation there to apply to the B2B vertical?

A - Bracken Darrell {BIO 3403495 <GO>}

Okay. First, I would say we're trying to unlearn our consumer vertical into the B2B, because I think our strength in consumer is something that really doesn't lend itself to much to the B2B side right now. We've taken -- we leverage as much of that as we possibly could of during the first kind of five years or six years in the business and now we're building new vessel, which is how to be a B2B company. And I'm excited about our potential there. We have a long way to go to really I think first class -- in that space, but I think that's the upside here of, how do we become a great execution engine into B2B? So I think it's still early days in that path. We've got the right resources in place. We've got the right capacity. And we're putting step-by-step process -- thought process and compensation plans everything into place to really become stronger B2B. So, I keep asking this about that. I think it's more of the hotspot of our business and one of the areas as we improve, I think, we can improve our performance.

Q - George Wang {BIO 17439572 <GO>}

Yeah. Maybe you could unpack a little bit in terms of the installed base and refresh slash that kind of upgrade cycle, kind of against this if you macro -- if the economy were to slow further. How do you think this installed base refresh going to play out? Do you think that's going to be delayed or do you think it's just a more temporal kind of headwind there?

A - Bracken Darrell {BIO 3403495 <GO>}

You're talking about on the desktop side? I mean, --

Q - George Wang {BIO 17439572 <GO>}

Yeah, just across the portfolio kind of mostly on the PC installed base also on the kb as well.

A - Bracken Darrell {BIO 3403495 <GO>}

I think if there is -- if there is a dramatic slowdown, it goes out for a long time. It certainly -- it is going to delay the installed base refresh across almost every category you can think of in the world, including probably ours. But -- but I think ours are -- if you look at our products, whether it's personal workspace video they kind of are required for the new

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world we're in. So I'm not sure that you can -- in the office, for example, Video Collaboration, while there may be a delay, it feels like there is short term, which really hard to imagine that last thing a really long time because in a hybrid world where you're doing so much video like we are all right now, it's really hard to imagine that video enablement of room. So I think that's -- I think -- I'm pretty positive on that yet. Could be, it could be some kind of a delay in that, it looks like there was this quarter. But I don't know how long that can go on. We'll see. On the -- on the workspace side, this is so central to what we do now. Everybody in this call sitting in front of the desktop with some stuff in front of them. And I would guess 90% of you don't have really exactly what you need, even if you don't realize quite yet. So I think that upgrade cycle is coming. And it's already started and it will continue for a very long time. And maybe if you're really about -- I'll stay away from -- going too far on this. But I think you can imagine it's become more central to our lives as part of our homes and things. So the upgraded cycle could even accelerate. But I think -- regardless, I think there's a good strong upgraded cycle ahead of us and could it be slowed down a little bit? Yes. Will it be stopped? No.

Q - George Wang {BIO 17439572 <GO>}

Yeah. I'd like to squeeze in my last question, if I may. Can you give more color and impact a little bit in terms of the recent market share gains across key categories? That's super encouraging. It seems largest outgrowing the industry. There used to be levers and the differentiation, you guys have to -- for this to sustain the kind of market share gains.

A - Bracken Darrell {BIO 3403495 <GO>}

We announced last quarter -- we have launched 20 or announced 20 new products. It's kind of a reflection. Numbers don't tell the whole story course. We're actually trying to fewer bigger, but -- but I think it's kind of a reflection of our investment. We started nine or 10 years ago really focusing on design, which means putting the user in the middle of the action. And we've really matured that approach. Meanwhile we kept investing in engineering over 50%, four years and in our total spending on engineering. And certainly the -- that's happening across all of our categories. So I feel very, very good about the innovation engine and is the primary driver of growth. But it's not the only one. The go-to-market in the B2B side is a big opportunity too, and we're going to keep investing there.

Q - George Wang {BIO 17439572 <GO>}

Thank you.

A - Nate Olmstead {BIO 21036514 <GO>}

Maybe, just wondering, you started to mention the go-to-market. I think some of the things that teams have been doing around analytics and in e-tail or on Amazon, I think have also continued to be really impressive. And our share numbers are really good at Amazon and across the categories. So I think, it does start with the products and you look at the ratings on the products and you can see those are quite good, George, but I also think that you have to (inaudible) go-to-market team with their work they're doing around analytics.

A - Bracken Darrell {BIO 3403495 <GO>}

Really good about that.

Q - George Wang {BIO 17439572 <GO>}

Great. Thank you.

A - Bracken Darrell {BIO 3403495 <GO>}

Thanks, George.

A - Nate Melihercik {BIO 20814398 <GO>}

Thanks, George. Our final question this morning is from Michael Foeth at Vontobel. Good morning, Michael.

A - Bracken Darrell {BIO 3403495 <GO>}

Hi, Michael.

Q - Michael Foeth

Hi. Thank you. Two questions from my side. If you could give some more color on the, on the appointment of Prakash to COO -- as COO position, sorry. And, sorry, what sort of gaps you think you need to fill there? What improvements you're seeing on the operation side? And the second question would be regarding your thoughts on the creator economy, as we go into recession. Do you see particular dynamics developing there? And and how you position yourselves to harness those opportunities?

A - Bracken Darrell {BIO 3403495 <GO>}

It's a really interesting question. And on Prakash -- Prakash has always been, I mean it's been here for seven years. We recruited him right out of a consulting firm and he has just grown and grown. And a lot of what you see from a sustainability standpoint, we're doing this company, you can -- you can put right Prakash's leadership. He has got a tremendous team. And in my entire staff a right alongside have been part of this drive to be better for the world from an environmental standpoint. But no mistake Prakash has led from the heart and the hands -- and head. But I think the next step for him and for us is to give him a larger role, not only in the overall operating execution of the company, but also in the structure and the cost of the company. And so this is another -- this is -- we're continuing -- we've evolved very quickly structurally, very quietly. Behind the scenes, we've changed our structure and we're gonna keep evolving it going forward. We will just keep evolving and he is going to be a real partner for me and for the CFO, and for the whole team in helping think through that. So think of him as overseeing the overall operating costs of the company. He also has responsibility for the overall M&A strategy Corp Dev. So he's got a big chunk of responsibility. And there are others, who have huge chunk of responsibility to only focus on Prakash, but we did announce this move today. So it's a big one. On the creator economy, recession and what are our prospects going forward, the creator economy touching so many things. I think it's one of the quiet drivers of interest in the personal workspaces we follow, mice, keyboards, webcams et cetera. That's said, it's one of quite drivers of that business. And I think -- it's here to stay the growth of all the things we read about, including the new world of ChatGPT and what that can unlock. I think all

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these are fuel for that creator economy. Now, I do think -- if you go into a deeper recession, I think the creator economy will -- lot of those people will end up in full-time jobs, if they weren't already in them, are trying to get full-time jobs, but they're going to keep going alongside that in this creator economy. And I think the other thing about the creator economy what's exciting to me is that I think more and more people are going to be selling to their friends directly. And we're experimenting with that lots of companies are I think there'll be more and more of that kind of selling. It's probably not going to be significant in the short term, but I think in the future, there will be more and more of a network of activity to drive sales through the creator economy that will be part of it.

Q - Michael Foeth

Thank you.

A - Nate Olmstead {BIO 21036514 <GO>}

Thanks, Michael.

A - Bracken Darrell {BIO 3403495 <GO>}

Thanks very much Michael.

A - Nate Melihercik {BIO 20814398 <GO>}

Thanks Michael and thanks everyone for joining. I think -- that's a wrap Nate and Bracken.

A - Bracken Darrell {BIO 3403495 <GO>}

Right. Thank you. Thanks everyone.

A - Nate Olmstead {BIO 21036514 <GO>}

Great. Thank you.

A - Bracken Darrell {BIO 3403495 <GO>}

Thank you. (inaudible) which will announce shortly.

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