

LULULEMON ATHLETICA INC.

FORM 10-Q (Quarterly Report)

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Telephone	604-732-6124
CIK	0001397187
Symbol	LULU
SIC Code	2300 - Apparel & Other Finishd Prods of Fabrics & Similar Matl
Industry	Apparel/Accessories
Sector	Consumer Cyclical
Fiscal Year	01/31

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

Form 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended July 31, 2016

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number 001-33608

lululemon athletica inc.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

**1818 Cornwall Avenue
Vancouver, British Columbia**
(Address of principal executive offices)

20-3842867

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

V6J 1C7
(Zip Code)

Registrant's telephone number, including area code:

604-732-6124

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

N/A

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

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

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

Large accelerated filer

Accelerated filer

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

Smaller reporting company

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

At August 29, 2016, there were 127,262,705 shares of the registrant's common stock, par value \$0.005 per share, outstanding.

Exchangeable and Special Voting Shares:

At August 29, 2016, there were outstanding 9,784,239 exchangeable shares of Lulu Canadian Holding, Inc., a wholly-owned subsidiary of the registrant. Exchangeable shares are exchangeable for an equal number of shares of the registrant's common stock.

In addition, at August 29, 2016, the registrant had outstanding 9,784,239 shares of special voting stock, through which the holders of exchangeable shares of Lulu Canadian Holding, Inc. may exercise their voting rights with respect to the registrant. The special voting stock and the registrant's common stock generally vote together as a single class on all matters on which the common stock is entitled to vote.

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PART I
FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

lululemon athletica inc.
CONSOLIDATED BALANCE SHEETS
(Unaudited; Amounts in thousands, except per share amounts)

	July 31, 2016	January 31, 2016
ASSETS		
Current assets		
Cash and cash equivalents	\$ 535,350	\$ 501,482
Accounts receivable	10,196	13,108
Inventories	277,279	284,009
Prepaid and receivable income taxes	98,678	91,453
Other prepaid expenses and other current assets	41,180	26,987
	962,683	917,039
Property and equipment, net	395,010	349,605
Goodwill and intangible assets, net	24,897	24,777
Deferred income tax assets	12,696	11,802
Other non-current assets	20,215	10,854
	\$ 1,415,501	\$ 1,314,077
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	\$ 8,295	\$ 10,381
Accrued inventory liabilities	19,287	25,451
Accrued compensation and related expenses	39,495	43,524
Income taxes payable	33,592	37,736
Unredeemed gift card liability	46,181	57,736
Other accrued liabilities	50,588	50,676
	197,438	225,504
Deferred income tax liabilities	11,198	10,759
Other non-current liabilities	50,663	50,332
	259,299	286,595
Stockholders' equity		
Undesignated preferred stock, \$0.01 par value: 5,000 shares authorized; none issued and outstanding	—	—
Exchangeable stock, no par value: 60,000 shares authorized; 9,784 and 9,804 issued and outstanding	—	—
Special voting stock, \$0.000005 par value: 60,000 shares authorized; 9,784 and 9,804 issued and outstanding	—	—
Common stock, \$0.005 par value: 400,000 shares authorized; 127,258 and 127,482 issued and outstanding	636	637
Additional paid-in capital	257,710	245,533
Retained earnings	1,090,549	1,019,515
Accumulated other comprehensive loss	(192,693)	(238,203)
	1,156,202	1,027,482
	\$ 1,415,501	\$ 1,314,077

See accompanying notes to the unaudited interim consolidated financial statements

lululemon athletica inc.
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
(Unaudited; Amounts in thousands, except per share amounts)

	Thirteen Weeks Ended July 31, 2016	Thirteen Weeks Ended August 2, 2015	Twenty-Six Weeks Ended July 31, 2016	Twenty-Six Weeks Ended August 2, 2015
Net revenue	\$ 514,520	\$ 453,010	\$ 1,010,036	\$ 876,554
Cost of goods sold	260,359	240,985	516,744	458,652
Gross profit	254,161	212,025	493,292	417,902
Selling, general and administrative expenses	180,202	145,446	361,744	283,287
Income from operations	73,959	66,579	131,548	134,615
Other income (expense), net	578	842	92	1,371
Income before income tax expense	74,537	67,421	131,640	135,986
Income tax expense	20,912	19,753	32,679	40,508
Net income	<u>\$ 53,625</u>	<u>\$ 47,668</u>	<u>\$ 98,961</u>	<u>\$ 95,478</u>
Other comprehensive (loss) income:				
Foreign currency translation adjustment	(28,052)	(39,368)	45,510	(16,762)
Comprehensive income	<u>\$ 25,573</u>	<u>\$ 8,300</u>	<u>\$ 144,471</u>	<u>\$ 78,716</u>
Basic earnings per share	\$ 0.39	\$ 0.34	\$ 0.72	\$ 0.67
Diluted earnings per share	\$ 0.39	\$ 0.34	\$ 0.72	\$ 0.67
Basic weighted-average number of shares outstanding	136,987	141,372	137,071	141,656
Diluted weighted-average number of shares outstanding	137,229	141,644	137,309	141,977

See accompanying notes to the unaudited interim consolidated financial statements

lululemon athletica inc.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited; Amounts in thousands)

	<u>Exchangeable Stock</u>	<u>Special Voting Stock</u>		<u>Common Stock</u>		<u>Additional Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Loss</u>	<u>Total</u>
	<u>Shares</u>	<u>Shares</u>	<u>Par Value</u>	<u>Shares</u>	<u>Par Value</u>				
Balance at January 31, 2016	9,804	9,804	\$ —	127,482	\$ 637	\$ 245,533	\$ 1,019,515	\$ (238,203)	\$ 1,027,482
Net income							98,961		98,961
Foreign currency translation adjustment								45,510	45,510
Common stock issued upon exchange of exchangeable shares	(20)	(20)	—	20	—	—			—
Stock-based compensation expense						8,126			8,126
Tax benefits from stock-based compensation						1,205			1,205
Common stock issued upon settlement of stock-based compensation				224	1	5,078			5,079
Shares withheld related to net share settlement of stock-based compensation				(25)	—	(1,605)			(1,605)
Repurchase of common stock				(443)	(2)	(627)	(27,927)		(28,556)
Balance at July 31, 2016	<u>9,784</u>	<u>9,784</u>	<u>\$ —</u>	<u>127,258</u>	<u>\$ 636</u>	<u>\$ 257,710</u>	<u>\$ 1,090,549</u>	<u>\$ (192,693)</u>	<u>\$ 1,156,202</u>

See accompanying notes to the unaudited interim consolidated financial statements

lululemon athletica inc.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited; Amounts in thousands)

	Twenty-Six Weeks Ended July 31, 2016	Twenty-Six Weeks Ended August 2, 2015
Cash flows from operating activities		
Net income	\$ 98,961	\$ 95,478
Items not affecting cash		
Depreciation and amortization	39,683	32,791
Stock-based compensation expense	8,126	6,021
Tax benefits from stock-based compensation	(1,205)	(649)
Changes in operating assets and liabilities		
Inventories	16,947	(74,010)
Prepaid and receivable income taxes	(6,020)	(13,614)
Other prepaid expenses and other current assets	(9,595)	(5,434)
Accounts payable	(2,512)	(1,809)
Accrued inventory liabilities	(8,432)	13,666
Accrued compensation and related expenses	(5,967)	3,394
Income taxes payable	(6,948)	(18,463)
Unredeemed gift card liability	(12,679)	(9,983)
Other accrued liabilities	(1,060)	2,828
Other non-current assets and liabilities	(9,311)	1,945
Net cash provided by operating activities	99,988	32,161
Cash flows from investing activities		
Purchase of property and equipment	(71,261)	(65,118)
Net cash used in investing activities	(71,261)	(65,118)
Cash flows from financing activities		
Proceeds from settlement of stock-based compensation	5,079	4,121
Tax benefits from stock-based compensation	1,205	649
Taxes paid related to net share settlement of stock-based compensation	(1,605)	(1,464)
Repurchase of common stock	(28,556)	(81,998)
Registration fees associated with prospectus supplement	—	(145)
Net cash used in financing activities	(23,877)	(78,837)
Effect of exchange rate changes on cash and cash equivalents	29,018	(11,423)
Increase (decrease) in cash and cash equivalents	33,868	(123,217)
Cash and cash equivalents, beginning of period	\$ 501,482	\$ 664,479
Cash and cash equivalents, end of period	\$ 535,350	\$ 541,262

See accompanying notes to the unaudited interim consolidated financial statements

lululemon athletica inc.
NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Nature of operations

lululemon athletica inc., a Delaware corporation ("lululemon" and, together with its subsidiaries unless the context otherwise requires, the "Company") is engaged in the design, distribution, and retail of healthy lifestyle inspired athletic apparel, which is sold through a chain of company-operated stores, direct to consumer through e-commerce, outlets, showrooms, sales to wholesale accounts, warehouse sales, temporary locations, and through a license and supply arrangement. The Company operates stores in the United States, Canada, Australia, the United Kingdom, New Zealand, Singapore, Hong Kong, Germany, Puerto Rico, South Korea, and Switzerland. There were a total of 379 and 363 company-operated stores in operation as of July 31, 2016 and January 31, 2016, respectively.

Basis of presentation

The unaudited interim consolidated financial statements as of July 31, 2016 and for the thirteen and twenty-six weeks ended July 31, 2016 and August 2, 2015 are presented in United States dollars and have been prepared by the Company under the rules and regulations of the Securities and Exchange Commission ("SEC"). The financial information is presented in accordance with United States generally accepted accounting principles ("GAAP") for interim financial information and, accordingly, does not include all of the information and footnotes required by GAAP for complete financial statements. The financial information as of January 31, 2016 is derived from the Company's audited consolidated financial statements and related notes for the fiscal year ended January 31, 2016, which are included in Item 8 in the Company's fiscal 2015 Annual Report on Form 10-K filed with the SEC on March 30, 2016. These unaudited interim consolidated financial statements reflect all adjustments which are, in the opinion of management, necessary to a fair statement of the results for the interim periods presented. These unaudited interim consolidated financial statements should be read in conjunction with the Company's consolidated financial statements and related notes included in Item 8 in the Company's fiscal 2015 Annual Report on Form 10-K.

The Company's fiscal year ends on the Sunday closest to January 31 of the following year, typically resulting in a 52-week year, but occasionally giving rise to an additional week, resulting in a 53-week year. Fiscal 2016 will end on January 29, 2017 and will be a 52-week year.

The Company's business is affected by the pattern of seasonality common to most retail apparel businesses. Historically, the Company has recognized a significant portion of its operating profit in the fourth fiscal quarter of each year as a result of increased net revenue during the holiday season.

Certain comparative figures have been reclassified to conform to the financial presentation adopted for the current year.

NOTE 2. RECENT ACCOUNTING PRONOUNCEMENTS

In May 2014, the Financial Accounting Standards Board ("FASB") issued ASC Topic 606, *Revenue from Contracts with Customers* ("ASC 606"), which supersedes the revenue recognition requirements in ASC Topic 605 *Revenue Recognition*, including most industry-specific revenue recognition guidance throughout the Industry Topics of the Codification. This guidance requires that an entity recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services, and expands the related disclosure requirements. In 2015, the FASB deferred the effective date for this guidance, and in 2016, the FASB issued several updates that clarify the guidance in this topic. This guidance will be effective for the Company beginning in its first quarter of fiscal 2018, with early application permitted if adopted in its first quarter of fiscal 2017. The Company is currently evaluating the timing of adoption and the impact that this new guidance may have on its consolidated financial statements.

In June 2014, the FASB amended ASC Topic 718, *Compensation - Stock Compensation* ("ASC 718") for share-based payments in which the terms of the award provide that a performance target can be achieved after the requisite service period. The amendments require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. This guidance became effective for the Company beginning in its first quarter of fiscal 2016 and it was adopted prospectively. The adoption did not have an impact on the Company's consolidated financial statements.

In April 2015, the FASB amended ASC Subtopic 350-40, *Intangibles - Goodwill and Other - Internal-Use Software* ("ASC 350-40") to provide guidance to customers about whether a cloud computing arrangement includes a software license. This guidance requires that if a cloud computing arrangement includes a software license, the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. This guidance became effective for the Company beginning in its first quarter of fiscal 2016 and it was adopted prospectively. The adoption did not have a material impact on the Company's consolidated financial statements.

In July 2015, the FASB amended ASC Topic 330, *Inventory* ("ASC 330") to simplify the measurement of inventory. The amendments require that an entity measure inventory at the lower of cost and net realizable value instead of the lower of cost and market. This guidance will be effective for the Company beginning in its first quarter of fiscal 2017, with early application permitted. The Company is currently evaluating the impact that this new guidance may have on its consolidated financial statements.

In February 2016 the FASB issued ASC Topic 842, *Leases* ("ASC 842") to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. Under the new guidance, lessees are required to recognize a lease liability, which represents the discounted obligation to make future minimum lease payments, and a corresponding right-of-use asset on the balance sheet for most leases. This guidance will be effective for the Company beginning in its first quarter of fiscal 2019, with early application permitted. The Company is currently evaluating the impact that this new guidance will have on its consolidated financial statements but it is expected that the adoption will result in a significant increase in assets and liabilities on the consolidated balance sheets.

In March 2016, the FASB amended ASC 718, simplifying the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The new guidance also allows an entity to account for forfeitures when they occur. This guidance will be effective for the Company beginning in its first quarter of fiscal 2017, with early application permitted. The Company is currently evaluating the impact that this new guidance may have on its consolidated financial statements.

NOTE 3. STOCK-BASED COMPENSATION

Stock-based compensation plans

The Company's eligible employees participate in various stock-based compensation plans, which are provided by the Company directly.

Stock-based compensation expense charged to income for the plans was \$8.1 million and \$6.0 million for the twenty-six weeks ended July 31, 2016 and August 2, 2015, respectively. Total unrecognized compensation cost for all stock-based compensation plans was \$49.1 million at July 31, 2016, which is expected to be recognized over a weighted-average period of 2.5 years.

Company stock options, performance-based restricted stock units, restricted shares and restricted stock units

A summary of the Company's stock option, performance-based restricted stock unit, restricted share and restricted stock unit activity as of July 31, 2016, and changes during the twenty-six week period then ended is presented below:

	Stock Options		Performance-Based Restricted Stock Units		Restricted Shares		Restricted Stock Units	
	Number	Weighted-Average Exercise Price	Number	Weighted-Average Grant Date Fair Value	Number	Weighted-Average Grant Date Fair Value	Number	Weighted-Average Grant Date Fair Value
<i>(In thousands, except per share amounts)</i>								
Balance at January 31, 2016	867	\$ 49.54	395	\$ 58.58	31	\$ 57.67	333	\$ 55.91
Granted	406	68.68	156	68.68	17	69.94	187	68.49
Exercised/vested	152	33.43	4	64.96	18	65.73	51	63.91
Forfeited	122	57.51	134	62.74	—	—	60	52.91
Balance at July 31, 2016	999	\$ 58.79	413	\$ 60.98	30	\$ 59.75	409	\$ 61.12
Exercisable at July 31, 2016	163	\$ 50.34						

The fair value of each stock option granted is estimated on date of grant using the Black-Scholes model. The assumptions used to calculate the fair value of options granted are evaluated and revised, as necessary, to reflect market conditions and the Company's historical experience. The expected term of the options is based upon historical experience of similar awards, giving consideration to expectations of future employee behavior. Expected volatility is based upon the historical volatility of the Company's common stock for the period corresponding with the expected term of the options. The risk-free interest rate is based on the U.S. Treasury yield curve for the period corresponding with the expected term of the options. The following assumptions were used in calculating the fair value of stock options granted in fiscal 2016 :

	Stock Options Granted During Fiscal 2016
Expected term	4 years
Expected volatility	40.07%
Risk-free interest rate	1.08%
Dividend yield	—%

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

The fair value of the restricted shares and restricted stock units is based on the closing price of the Company's common stock on the award date.

Employee share purchase plan

The Company's board of directors and stockholders approved the Company's Employee Share Purchase Plan ("ESPP") in September 2007. Contributions are made by eligible employees, subject to certain limits defined in the ESPP, and the Company matches one-third of the contribution. The maximum number of shares available under the ESPP is 6.0 million shares. During the thirteen weeks ended July 31, 2016, there were 31.6 thousand shares purchased in the open market under the ESPP.

NOTE 4. EARNINGS PER SHARE

The details of the computation of basic and diluted earnings per share are as follows:

	Thirteen Weeks Ended July 31, 2016	Thirteen Weeks Ended August 2, 2015	Twenty-Six Weeks Ended July 31, 2016	Twenty-Six Weeks Ended August 2, 2015
	<i>(In thousands, except per share amounts)</i>			
Net income	\$ 53,625	\$ 47,668	\$ 98,961	\$ 95,478
Basic weighted-average number of shares outstanding	136,987	141,372	137,071	141,656
Assumed conversion of dilutive stock options and awards	242	272	238	321
Diluted weighted-average number of shares outstanding	137,229	141,644	137,309	141,977
Basic earnings per share	\$ 0.39	\$ 0.34	\$ 0.72	\$ 0.67
Diluted earnings per share	\$ 0.39	\$ 0.34	\$ 0.72	\$ 0.67

The Company's calculation of weighted-average shares includes the common stock of the Company as well as the exchangeable shares. Exchangeable shares are the equivalent of common shares in all material respects. All classes of stock have, in effect, the same rights and share equally in undistributed net income. For each of the twenty-six weeks ended July 31, 2016 and August 2, 2015, 0.1 million stock options and awards were anti-dilutive to earnings per share and therefore have been excluded from the computation of diluted earnings per share.

On June 11, 2014, the Company's board of directors approved a program to repurchase shares of the Company's common stock up to an aggregate value of \$450.0 million. The common stock was repurchased in the open market at prevailing market prices, with the timing and actual number of shares repurchased depending upon market conditions and other factors. During the twenty-six weeks ended July 31, 2016 and August 2, 2015, 0.4 million and 1.3 million shares, respectively, were repurchased under the program at a total cost of \$28.6 million and \$82.0 million, respectively. The Company's stock repurchase program was completed during the second quarter of fiscal 2016.

NOTE 5. SUPPLEMENTARY FINANCIAL INFORMATION

For the thirteen weeks ended July 31, 2016 and August 2, 2015, there were net foreign exchange gains of \$5.1 million and \$5.6 million, respectively, included within selling, general and administrative expenses.

For the twenty-six weeks ended July 31, 2016 and August 2, 2015, there were net foreign exchange losses of \$8.5 million and net foreign exchange gains of \$1.2 million, respectively, included within selling, general and administrative expenses.

A summary of certain consolidated balance sheet accounts is as follows:

	July 31, 2016	January 31, 2016
(In thousands)		
Inventories:		
Finished goods	\$ 285,909	\$ 290,791
Provision to reduce inventory to market value	(8,630)	(6,782)
	<u>\$ 277,279</u>	<u>\$ 284,009</u>
Property and equipment, net:		
Land	\$ 78,922	\$ 55,488
Buildings	32,642	30,885
Leasehold improvements	248,223	225,604
Furniture and fixtures	79,856	73,254
Computer hardware	50,128	44,085
Computer software	136,941	112,161
Equipment and vehicles	12,675	11,929
Accumulated depreciation	(244,377)	(203,801)
	<u>\$ 395,010</u>	<u>\$ 349,605</u>
Goodwill and intangible assets, net:		
Goodwill	\$ 25,496	\$ 25,496
Changes in foreign currency exchange rates	(1,233)	(1,666)
	<u>24,263</u>	<u>23,830</u>
Intangibles—reacquired franchise rights	10,150	10,150
Accumulated amortization	(9,466)	(9,074)
Changes in foreign currency exchange rates	(50)	(129)
	<u>634</u>	<u>947</u>
	<u>\$ 24,897</u>	<u>\$ 24,777</u>
Other accrued liabilities:		
Accrued duty, freight, and other operating expenses	\$ 27,794	\$ 26,017
Sales tax collected	9,632	10,506
Accrued rent	6,067	6,070
Other	7,095	8,083
	<u>\$ 50,588</u>	<u>\$ 50,676</u>
Other non-current liabilities:		
Deferred lease liability	\$ 26,945	\$ 25,723
Tenant inducements	23,718	24,609
	<u>\$ 50,663</u>	<u>\$ 50,332</u>

NOTE 6. LEGAL PROCEEDINGS

In addition to the legal matters described below, the Company is, from time to time, involved in routine legal matters incidental to the conduct of its business, including legal matters such as initiation and defense of proceedings to protect intellectual property rights, personal injury claims, product liability claims, and similar matters. The Company believes the ultimate resolution of any such current proceeding will not have a material adverse effect on its consolidated balance sheets, results of operations or cash flows.

On July 15, 2015, plaintiffs Hallandale Beach Police Officers and Firefighters' Personnel Retirement Fund and Laborers' District Council Industry Pension Fund filed in the Delaware Court of Chancery a derivative lawsuit on behalf of lululemon against certain current and former directors of lululemon, captioned *Laborers' District Council Industry Pension Fund v. Bensoussan, et al.*, C.A. No. 11293-CB. Plaintiffs claim that the individual defendants breached their fiduciary duties to lululemon by allegedly failing to investigate certain trades of lululemon stock owned by Dennis J. Wilson in 2013. Plaintiffs

also claim that Mr. Wilson breached his fiduciary duties by making his broker aware of certain non-public, material events prior to executing sales of lululemon stock on Mr. Wilson's behalf. On June 14, 2016 the Court dismissed the action for failure to adequately plead that demand on the board was excused and for failure to state a claim upon which relief may be granted. The plaintiffs have appealed the dismissal to the Supreme Court of the state of Delaware.

On October 9, 2015, certain current and former hourly employees of the Company filed a class action lawsuit in the Supreme Court of New York entitled *Rebecca Gathmann-Landini et al v. lululemon USA inc.* On December 2, 2015, the case was moved to the United States District Court for the Eastern District of New York. The lawsuit alleges that the Company violated various New York labor codes by failing to pay all earned wages, including overtime compensation. The plaintiffs are seeking an unspecified amount of damages. The Company intends to vigorously defend this matter.

NOTE 7. INCOME TAXES

The Company is in the process of finalizing a bilateral Advance Pricing Arrangement ("APA") with the Internal Revenue Service ("IRS") and the Canada Revenue Agency ("CRA"), as detailed in Note 15 included in Item 8 of the Company's fiscal 2015 Annual Report on Form 10-K filed with the SEC on March 30, 2016 .

The outcome of the APA will result in an income tax recovery in the United States and an income tax payment in Canada for fiscal 2011 through fiscal 2015.

During the first quarter of fiscal 2016 , the Company received new communications from the IRS with respect to the APA. Based on this new information, the Company has determined that it is now more likely than not that the APA will result in an increased amount of income tax recoverable in the United States for fiscal 2011 through fiscal 2015. The Company also updated its income tax calculations with respect to the APA and the associated plan to repatriate \$156.0 million of foreign earnings, for the exchange rates in effect as of July 31, 2016 . These income tax adjustments resulted in a net income tax recovery of \$1.9 million in the second quarter of fiscal 2016 , and \$7.6 million in the first two quarters of fiscal 2016 .

The Company recorded a related net interest expense of \$0.3 million in the second quarter of fiscal 2016 in other income (expense), net, and \$1.5 million in the first two quarters of fiscal 2016 . This primarily represents additional accrued interest on the Canadian income tax payable related to the APA.

The Company anticipates that the APA will be finalized within the next six months. The Company's expected filing position represents the largest benefit considered by management to be more likely than not. However, the Company's tax position will be updated as new information becomes available.

NOTE 8. SEGMENT REPORTING

The Company applies ASC Topic 280, *Segment Reporting* ("ASC 280"), in determining reportable segments for its financial statement disclosure. The Company reports segments based on the financial information it uses in managing its business. The Company's reportable segments are comprised of company-operated stores and direct to consumer. Direct to consumer represents sales from the Company's e-commerce websites. Outlets, showrooms, sales to wholesale accounts, warehouse sales, temporary locations, and a license and supply arrangement have been combined into other. Information for these segments is detailed in the table below:

	Thirteen Weeks Ended July 31, 2016	Thirteen Weeks Ended August 2, 2015	Twenty-Six Weeks Ended July 31, 2016	Twenty-Six Weeks Ended August 2, 2015
<i>(In thousands)</i>				
Net revenue:				
Company-operated stores	\$ 381,389	\$ 339,779	\$ 740,093	\$ 653,873
Direct to consumer	87,399	82,239	184,965	165,875
Other	45,732	30,992	84,978	56,806
	<u>\$ 514,520</u>	<u>\$ 453,010</u>	<u>\$ 1,010,036</u>	<u>\$ 876,554</u>
Income from operations before general corporate expense:				
Company-operated stores	\$ 80,277	\$ 67,441	\$ 153,564	\$ 136,664
Direct to consumer	32,644	32,250	71,152	67,121
Other	4,636	1,820	6,720	2,801
	<u>117,557</u>	<u>101,511</u>	<u>231,436</u>	<u>206,586</u>
General corporate expense	43,598	34,932	99,888	71,971
Income from operations	73,959	66,579	131,548	134,615
Other income (expense), net	578	842	92	1,371
Income before income tax expense	<u>\$ 74,537</u>	<u>\$ 67,421</u>	<u>\$ 131,640</u>	<u>\$ 135,986</u>
Capital expenditures:				
Company-operated stores	\$ 11,515	\$ 24,788	\$ 28,265	\$ 41,632
Direct to consumer	4,551	1,479	5,715	1,932
Corporate and other	28,552	10,915	37,281	21,554
	<u>\$ 44,618</u>	<u>\$ 37,182</u>	<u>\$ 71,261</u>	<u>\$ 65,118</u>
Depreciation and amortization:				
Company-operated stores	\$ 14,511	\$ 11,736	\$ 28,295	\$ 23,013
Direct to consumer	1,725	1,599	3,054	3,135
Corporate and other	4,261	3,360	8,334	6,643
	<u>\$ 20,497</u>	<u>\$ 16,695</u>	<u>\$ 39,683</u>	<u>\$ 32,791</u>

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

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

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

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

This information should be read in conjunction with the unaudited interim consolidated financial statements and the notes included in Item 1 of Part I of this Quarterly Report on Form 10-Q and the audited consolidated financial statements and notes, and Management's Discussion and Analysis of Financial Condition and Results of Operations, contained in our Annual Report on Form 10-K.

We disclose material non-public information through one or more of the following channels: our investor relations website (<http://investor.lululemon.com/>), the social media channels identified on our investor relations website, press releases, SEC filings, public conference calls, and webcasts.

Overview

lululemon is a designer, distributor, and retailer of healthy lifestyle inspired athletic apparel. Since our inception, we have developed a distinctive corporate culture, and we have a mission to produce products which create transformational experiences for people to live happy, healthy, fun lives. We promote a set of core values in our business which include taking personal responsibility, nurturing entrepreneurial spirit, acting with honesty and courage, valuing connection, and choosing to have fun. These core values attract passionate and motivated employees who are driven to succeed and share our purpose of "elevating the world from mediocrity to greatness."

Our healthy lifestyle inspired athletic apparel is marketed under the lululemon athletica and ivivva athletica brand names. We offer a comprehensive line of apparel and accessories for women, men and female youth. Our apparel assortment includes items such as pants, shorts, tops and jackets designed for healthy lifestyle and athletic activities such as yoga, running, training, most other sweaty pursuits, and athletic wear for female youth.

Financial Highlights

- Net revenue for second quarter of fiscal 2016 increased by 14% to \$514.5 million, from \$453.0 million in the second quarter of fiscal 2015. Net revenue increased across all segments, and the increase was primarily due to the addition of 43 net new company-operated stores since the second quarter of fiscal 2015, as well as increased comparable store sales.
- Total comparable sales, which includes comparable store sales and direct to consumer, increased 4% in the second quarter of fiscal 2016 compared to the second quarter of fiscal 2015. On a constant dollar basis, total comparable sales increased by 5%.
- Company-operated stores accounted for 74.1% of net revenue in the second quarter of fiscal 2016 compared to 75.0% of net revenue in the second quarter of fiscal 2015. Comparable store sales increased by 3% in the second quarter of fiscal

2016 compared to the second quarter of fiscal 2015 , or by 4% on a constant dollar basis, primarily as a result of improved conversion rates and increased dollar value per transaction.

- Our direct to consumer segment represented 17.0% of our net revenue in the second quarter of fiscal 2016 compared to 18.2% in the second quarter of fiscal 2015 . Direct to consumer net revenue increased by 6% in the second quarter of fiscal 2016 compared to the second quarter of fiscal 2015 , or by 7% on a constant dollar basis, primarily as the result of higher traffic on our e-commerce websites and increased dollar value per transaction. During the second quarter of fiscal 2015 , we held online warehouse sales in Canada and the United States which generated net revenue of \$6.6 million. We did not hold any online warehouse sales during the second quarter of fiscal 2016 .
- Gross profit for the second quarter of fiscal 2016 increase d by 20% to \$254.2 million , from \$212.0 million in the second quarter of fiscal 2015 . Gross profit as a percentage of net revenue, or gross margin, increase d to 49.4% compared to 46.8% in the second quarter of fiscal 2015 . The increase in gross margin was primarily due to lower product costs, partially offset by increased fixed costs and expenses related to our product and supply chain departments.
- Income from operations for the second quarter of fiscal 2016 increase d by 11% to \$74.0 million , from \$66.6 million in the second quarter of fiscal 2015 . As a percentage of net revenue, income from operations decreased to 14.4% compared to 14.7% of net revenue in the second quarter of fiscal 2015 .
- Income tax expense for the second quarter of fiscal 2016 increase d by 6% to \$20.9 million , from \$19.8 million in the second quarter of fiscal 2015 . Our effective tax rate for the second quarter of fiscal 2016 was 28.1% compared to 29.3% for the second quarter of fiscal 2015 . The second quarter of fiscal 2016 included a net income tax recovery of \$1.9 million related to our transfer pricing arrangements and the associated plan to repatriate foreign earnings. In addition, the second quarter of fiscal 2016 included a related net interest expense of \$0.3 million recorded in other income (expense), net. Our effective tax rate excluding these adjustments was 30.5% in the second quarter of fiscal 2016 .
- Diluted earnings per share for the second quarter of fiscal 2016 were \$0.39 compared to \$0.34 in the second quarter of fiscal 2015 . Excluding the above tax and related interest adjustments, diluted earnings per share were \$0.38 for the second quarter of fiscal 2016 .

Refer to the non-GAAP reconciliation tables contained in the "Results of Operations" section of this Management's Discussion and Analysis of Financial Condition and Results of Operations for reconciliations between constant dollar changes in net revenue, total comparable sales, comparable store sales, and direct to consumer net revenue, and the effective tax rate and diluted earnings per share excluding certain tax and related interest adjustments, and the most directly comparable measures calculated in accordance with GAAP.

Results of Operations

Thirteen Week Results

The following table summarizes key components of our results of operations for the thirteen weeks ended July 31, 2016 and August 2, 2015. The percentages are presented as a percentage of net revenue.

	Thirteen Weeks Ended July 31, 2016 and August 2, 2015			
	2016		2015	
	<i>(In thousands)</i>		<i>(Percentages)</i>	
Net revenue	\$ 514,520	\$ 453,010	100.0%	100.0%
Cost of goods sold	260,359	240,985	50.6	53.2
Gross profit	254,161	212,025	49.4	46.8
Selling, general and administrative expenses	180,202	145,446	35.0	32.1
Income from operations	73,959	66,579	14.4	14.7
Other income (expense), net	578	842	0.1	0.2
Income before income tax expense	74,537	67,421	14.5	14.9
Income tax expense	20,912	19,753	4.1	4.4
Net income	\$ 53,625	\$ 47,668	10.4%	10.5%

Net Revenue

Net revenue increased \$61.5 million, or 14%, to \$514.5 million for the second quarter of fiscal 2016 from \$453.0 million for the second quarter of fiscal 2015. On a constant dollar basis, assuming the average exchange rates for the second quarter of fiscal 2016 remained constant with the average exchange rates for the second quarter of fiscal 2015, net revenue increased \$66.8 million, or 15%.

Net revenue increased across all segments, and the increase was primarily from our company-operated stores, including net revenue from new stores and increased comparable store sales. Total comparable sales, which includes comparable store sales and direct to consumer, increased 4% in the second quarter of fiscal 2016 compared to the second quarter of fiscal 2015. Total comparable sales increased 5% on a constant dollar basis.

Our net revenue on a segment basis for the thirteen weeks ended July 31, 2016 and August 2, 2015 is summarized below. The percentages are presented as a percentage of total net revenue.

	Thirteen Weeks Ended July 31, 2016 and August 2, 2015			
	2016		2015	
	<i>(In thousands)</i>		<i>(Percentages)</i>	
Company-operated stores	\$ 381,389	\$ 339,779	74.1%	75.0%
Direct to consumer	87,399	82,239	17.0	18.2
Other	45,732	30,992	8.9	6.8
Net revenue	\$ 514,520	\$ 453,010	100.0%	100.0%

Company-operated Stores. Net revenue from our company-operated stores segment increased \$41.6 million, or 12%, to \$381.4 million in the second quarter of fiscal 2016 from \$339.8 million in the second quarter of fiscal 2015. The following contributed to the increase in net revenue from our company-operated stores segment:

- Net revenue from company-operated stores we opened or significantly expanded subsequent to August 2, 2015, and therefore not included in comparable store sales, contributed \$31.2 million to the increase. We have opened 43 net new company-operated stores since the second quarter of fiscal 2015, including 32 stores in the United States, two stores in each of Canada and the United Kingdom, and one store in each of Australia, Germany, Hong Kong, Puerto Rico, Singapore, South Korea, and Switzerland.
- A comparable store sales increase of 3% in the second quarter of fiscal 2016 compared to the second quarter of fiscal 2015 resulted in a \$10.4 million increase to net revenue. Comparable store sales increased 4%, or \$13.6 million on a constant dollar basis. The increase in comparable store sales was primarily as a result of improved conversion rates and increased dollar value per transaction.

Direct to Consumer. Net revenue from our direct to consumer segment increased \$5.2 million, or 6%, to \$87.4 million in the second quarter of fiscal 2016 from \$82.2 million in the second quarter of fiscal 2015. Direct to consumer revenue increased 7% on a constant dollar basis. This increase was primarily the result of higher traffic on our e-commerce websites and increased dollar value per transaction. During the second quarter of fiscal 2015, we held online warehouse sales in Canada and the United States which generated net revenue of \$6.6 million. We did not hold any online warehouse sales during the second quarter of fiscal 2016.

Other. Net revenue from our other segment increased \$14.7 million, or 48%, to \$45.7 million in the second quarter of fiscal 2016 from \$31.0 million in the second quarter of fiscal 2015. This increase was primarily the result of an increased number of outlets and increased revenue at existing outlets during the second quarter of fiscal 2016 compared to the second quarter of fiscal 2015, as well as net revenue from warehouse sales held during the second quarter of fiscal 2016.

Gross Profit

Gross profit increased \$42.1 million, or 20%, to \$254.2 million for the second quarter of fiscal 2016 from \$212.0 million for the second quarter of fiscal 2015.

Gross profit as a percentage of net revenue, or gross margin, increased by 260 basis points, to 49.4% in the second quarter of fiscal 2016 from 46.8% in the second quarter of fiscal 2015. The increase in gross margin was primarily the result of:

- lower product costs and lower costs related to our raw material commitments of 310 basis points; and
- a decrease in markdowns and discounts of 50 basis points.

This was offset by an increase in fixed costs, such as occupancy costs and depreciation, relative to the increase in net revenue, of 40 basis points, an increase in expenses related to our product and supply chain departments, relative to the increase in net revenue, of 40 basis points, and an unfavorable impact of foreign exchange rates of 20 basis points.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased \$34.8 million, or 24%, to \$180.2 million in the second quarter of fiscal 2016 from \$145.4 million in the second quarter of fiscal 2015. The increase in selling, general and administrative expenses was principally comprised of:

- an increase in employee costs for our operating locations of \$12.1 million primarily from a growth in labor hours and bonuses, mainly associated with new company-operated stores and other new operating locations;
- an increase in head office employee costs of \$10.8 million primarily due to additional employees to support the growth in our business;
- an increase in head office costs other than employee costs of \$4.7 million primarily due to increased professional fees, including supply chain consulting, increased information technology costs, increased depreciation, and increased brand and community costs;
- an increase in other costs of \$4.5 million for our operating channels including digital marketing expenses and repairs and maintenance costs;
- an increase in variable costs of \$2.2 million for our operating channels such as distribution costs and credit card fees, primarily as a result of increased sales; and
- a decrease in net foreign exchange gains of \$0.5 million, from \$5.6 million in the second quarter of fiscal 2015 to \$5.1 million in the second quarter of fiscal 2016, primarily related to the revaluation of U.S. dollar cash and receivables held in Canada.

As a percentage of net revenue, selling, general and administrative expenses increased 290 basis points, to 35.0% in the second quarter of fiscal 2016 from 32.1% in the second quarter of fiscal 2015.

Income from Operations

Income from operations increased \$7.4 million, or 11%, to \$74.0 million in the second quarter of fiscal 2016 from \$66.6 million in the second quarter of fiscal 2015. The increase was primarily the result of an increase in gross profit of \$42.1 million, partially offset by an increase in selling, general and administrative costs of \$34.8 million.

On a segment basis, we determine income from operations without taking into account our general corporate expenses.

Income from operations before general corporate expenses for the thirteen weeks ended July 31, 2016 and August 2, 2015 is summarized below. The percentages are presented as a percentage of net revenue of the respective operating segments.

	Thirteen Weeks Ended July 31, 2016 and August 2, 2015			
	2016		2015	
	(In thousands)		(Percentages)	
Company-operated stores	\$ 80,277	\$ 67,441	21.0%	19.8%
Direct to consumer	32,644	32,250	37.4	39.2
Other	4,636	1,820	10.1	5.9
Income from operations before general corporate expense	117,557	101,511		
General corporate expense	43,598	34,932		
Income from operations	\$ 73,959	\$ 66,579		

Company-operated Stores. Income from operations from our company-operated stores segment increased \$12.8 million, or 19%, to \$80.3 million for the second quarter of fiscal 2016 from \$67.4 million for the second quarter of fiscal 2015 primarily due to increased gross profit of \$29.1 million. This was partially offset by an increase in selling, general and administrative expenses, including increased store employee costs and higher operating expenses associated with new stores and increased net revenue at existing stores. Income from operations as a percentage of company-operated stores revenue increased by 120 basis points primarily due to increased gross margin, partially offset by deleverage of selling, general and administrative expenses.

Direct to Consumer. Income from operations from our direct to consumer segment increased \$0.4 million, or 1%, to \$32.6 million for the second quarter of fiscal 2016 from \$32.3 million for the second quarter of fiscal 2015. The increase was primarily the result of increased gross profit of \$7.3 million due to increased net revenue resulting from higher traffic on our e-commerce websites and increased dollar value per transaction. This was partially offset by an increase in selling, general and administrative expenses including higher digital marketing expenses and higher variable costs such as distribution and packaging as a result of higher net revenue. Income from operations as a percentage of direct to consumer revenue decreased by 180 basis points primarily due to deleverage of selling, general and administrative expenses, partially offset by increased gross margin.

Other. Other income from operations increased \$2.8 million, or 155%, to \$4.6 million for the second quarter of fiscal 2016 from \$1.8 million for the second quarter of fiscal 2015. The increase was primarily the result of increased gross profit of \$5.8 million, partially offset by increased selling, general and administrative expenses primarily due to increased employee costs. Income from operations as a percentage of other net revenue increased by 420 basis points primarily due to decreased selling, general and administrative expenses as a percentage of other net revenue.

General Corporate Expense. General corporate expense increased \$8.7 million, or 25%, to \$43.6 million for the second quarter of fiscal 2016 from \$34.9 million for the second quarter of fiscal 2015. This was primarily due to increased employee costs, professional fees, including increased professional fees related to supply chain consulting, and investment in strategic initiatives and projects to support the growth of our business. There was also a decrease in net foreign exchange gains of \$0.5 million, primarily related to the revaluation of U.S. dollar cash and receivables held in Canada.

Other Income (Expense), Net

Other income (expense), net, decreased \$0.3 million, or 31%, to \$0.6 million for the second quarter of fiscal 2016 from \$0.8 million for the second quarter of fiscal 2015. The decrease was primarily due to a net interest expense of \$0.3 million related to certain tax adjustments that are outlined in Note 7 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report.

Income Tax Expense

Income tax expense increased \$1.2 million, or 6%, to \$20.9 million in the second quarter of fiscal 2016 from \$19.8 million in the second quarter of fiscal 2015. The second quarter of fiscal 2016 included certain tax adjustments totaling a recovery of \$1.9 million as outlined in Note 7 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report.

The effective tax rate in the second quarter of fiscal 2016 was 28.1% compared to 29.3% in the second quarter of fiscal 2015. The effective tax rate excluding the above tax and related interest adjustments was 30.5% in the second quarter of fiscal 2016.

Net Income

Net income increased \$6.0 million, or 12%, to \$53.6 million for the second quarter of fiscal 2016 from \$47.7 million for the second quarter of fiscal 2015. The increase in net income was primarily the result of an increase in gross profit of \$42.1 million, partially offset by an increase in selling, general and administrative expenses of \$34.8 million, an increase in income tax expense of \$1.2 million, and a decrease in other income (expense), net of \$0.3 million.

Twenty-Six Week Results

The following table summarizes key components of our results of operations for the twenty-six week periods ended July 31, 2016 and August 2, 2015. The percentages are presented as a percentage of net revenue.

	Twenty-Six Weeks Ended July 31, 2016 and August 2, 2015			
	2016		2015	
	<i>(In thousands)</i>		<i>(Percentages)</i>	
Net revenue	\$ 1,010,036	\$ 876,554	100.0%	100.0%
Cost of goods sold	516,744	458,652	51.2	52.3
Gross profit	493,292	417,902	48.8	47.7
Selling, general and administrative expenses	361,744	283,287	35.8	32.3
Income from operations	131,548	134,615	13.0	15.4
Other income (expense), net	92	1,371	—	0.2
Income before income tax expense	131,640	135,986	13.0	15.6
Income tax expense	32,679	40,508	3.2	4.7
Net income	\$ 98,961	\$ 95,478	9.8%	10.9%

Net Revenue

Net revenue increased \$133.5 million, or 15%, to \$1,010.0 million for the first two quarters of fiscal 2016 from \$876.6 million for the first two quarters of fiscal 2015. On a constant dollar basis, assuming the average exchange rates for the first two quarters of fiscal 2016 remained constant with average exchange rates for the first two quarters of fiscal 2015, net revenue increased \$146.0 million, or 17%.

Net revenue increased across all segments, and the increase was primarily from our company-operated stores, including net revenue from new stores and increased comparable store sales. Total comparable sales, which includes comparable store sales and direct to consumer, increased 5% in the first two quarters of fiscal 2016 compared to the first two quarters of fiscal 2015. Total comparable sales increased 6% on a constant dollar basis.

Our net revenue on a segment basis for the twenty-six week periods ended July 31, 2016 and August 2, 2015 is summarized below. The percentages are presented as a percentage of total net revenue.

	Twenty-Six Weeks Ended July 31, 2016 and August 2, 2015			
	2016		2015	
	<i>(In thousands)</i>		<i>(Percentages)</i>	
Company-operated stores	\$ 740,093	\$ 653,873	73.3%	74.6%
Direct to consumer	184,965	165,875	18.3	18.9
Other	84,978	56,806	8.4	6.5
Net revenue	\$ 1,010,036	\$ 876,554	100.0%	100.0%

Company-operated Stores. Net revenue from our company-operated stores segment increased \$86.2 million, or 13%, to \$740.1 million in the first two quarters of fiscal 2016 from \$653.9 million in the first two quarters of fiscal 2015. The following contributed to the increase in net revenue from our company-operated stores segment:

- Net revenue from company-operated stores we opened or significantly expanded subsequent to August 2, 2015, and therefore not included in comparable store sales, contributed \$67.3 million to the increase. We have opened 43 net new company-operated stores since the second quarter of fiscal 2015, including 32 stores in the United States, two stores in each of Canada and the United Kingdom, and one store in each of Australia, Germany, Hong Kong, Puerto Rico, Singapore, South Korea, and Switzerland.

- A comparable store sales increase of 3% in the first two quarters of fiscal 2016 compared to the first two quarters of fiscal 2015 resulted in an \$18.9 million increase to net revenue. Comparable store sales increased 4% , or \$26.6 million on a constant dollar basis. The increase in comparable store sales was primarily as a result of improved conversion rates and increased dollar value per transaction.

Direct to Consumer. Net revenue from our direct to consumer segment increased \$19.1 million , or 12% , to \$185.0 million in the first two quarters of fiscal 2016 from \$165.9 million in the first two quarters of fiscal 2015 . Direct to consumer revenue increased 13% on a constant dollar basis. The increase in net revenue was primarily the result of higher traffic on our e-commerce websites and an increase in dollar value per transaction.

Other. Other net revenue increased \$28.2 million , or 50% , to \$85.0 million in the first two quarters of fiscal 2016 from \$56.8 million in the first two quarters of fiscal 2015 . This increase was primarily the result of an increased number of outlets and increased revenue at existing outlets during the first two quarters of fiscal 2016 compared to the first two quarters of fiscal 2015 , as well as net revenue from warehouse sales which were held during the second quarter of fiscal 2016 .

Gross Profit

Gross profit increased \$75.4 million , or 18% , to \$493.3 million for the first two quarters of fiscal 2016 from \$417.9 million for the first two quarters of fiscal 2015 .

Gross profit as a percentage of net revenue, or gross margin, increased by 110 basis points, to 48.8% in the first two quarters of fiscal 2016 from 47.7% in the first two quarters of fiscal 2015 . The increase in gross margin was primarily the result of an increase in product margin of 210 basis points, primarily due to lower product costs and lower costs related to our raw material commitments.

The increase in gross margin was partially offset by an unfavorable impact of foreign exchange rates of 50 basis points, an increase in fixed costs, such as occupancy costs and depreciation, relative to the increase in net revenue, of 30 basis points, and an increase in expenses related to our product and supply chain departments, relative to the increase in net revenue, of 20 basis points.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased \$78.5 million , or 28% , to \$361.7 million in the first two quarters of fiscal 2016 from \$283.3 million in the first two quarters of fiscal 2015 . The increase in selling, general and administrative expenses was principally comprised of:

- an increase in employee costs of \$24.8 million primarily from a growth in bonuses and labor hours associated with new company-operated stores and other new operating locations;
- an increase in head office employee costs of \$17.5 million primarily due to additional employees to support the growth in our business;
- an increase in head office costs other than employee costs of \$11.7 million primarily due to increased professional fees, including supply chain consulting, increased information technology costs, increased depreciation, and increased brand and community costs;
- an increase in net foreign exchange losses of \$9.6 million , from a net foreign exchange gain of \$1.2 million in the first two quarters of fiscal 2015 to a net foreign exchange loss of \$8.5 million in the first two quarters of fiscal 2016 , primarily related to the revaluation of U.S. dollar cash and receivables held in Canada;
- an increase in other costs of \$8.4 million for our operating channels such as digital marketing expenses, repairs and maintenance, utilities, and communication costs; and
- an increase in variable costs of \$6.5 million for our operating channels such as distribution costs, packaging, and credit card fees, primarily as a result of increased sales.

As a percentage of net revenue, selling, general and administrative expenses increased 350 basis points, to 35.8% in the first two quarters of fiscal 2016 from 32.3% in the first two quarters of fiscal 2015 .

Income from Operations

Income from operations decreased \$3.1 million , or 2% , to \$131.5 million in the first two quarters of fiscal 2016 from \$134.6 million in the first two quarters of fiscal 2015 . The decrease was primarily the result of an increase in selling, general and administrative costs of \$78.5 million , partially offset by increased gross profit of \$75.4 million .

On a segment basis, we determine income from operations without taking into account our general corporate expenses.

Income from operations before general corporate expenses for the twenty-six week periods ended July 31, 2016 and August 2, 2015 is summarized below. The percentages are presented as a percentage of net revenue of the respective operating segments.

	Twenty-Six Weeks Ended July 31, 2016 and August 2, 2015					
	2016		2015			
	<i>(In thousands)</i>		<i>(Percentages)</i>			
Company-operated stores	\$	153,564	\$	136,664	20.7%	20.9%
Direct to consumer		71,152		67,121	38.5	40.5
Other		6,720		2,801	7.9	4.9
Income from operations before general corporate expense		231,436		206,586		
General corporate expense		99,888		71,971		
Income from operations	\$	131,548	\$	134,615		

Company-operated Stores. Income from operations from our company-operated stores segment increased \$16.9 million , or 12% , to \$153.6 million for the first two quarters of fiscal 2016 from \$136.7 million for the first two quarters of fiscal 2015 primarily due to increase d gross profit of \$48.5 million . This was partially offset by an increase in selling, general and administrative expenses, including increased employee costs and increased operating expenses associated with new stores and increased net revenue at existing stores. Income from operations as a percentage of company-operated stores revenue decreased by 20 basis points, primarily due to deleverage of selling, general and administrative expenses, partially offset by an increase in gross margin.

Direct to Consumer. Income from operations from our direct to consumer segment increase d \$4.0 million , or 6% , to \$71.2 million for the first two quarters of fiscal 2016 from \$67.1 million for the first two quarters of fiscal 2015 . The increase was primarily the result of increase d gross profit of \$15.6 million primarily due to increased net revenue resulting from higher traffic on our e-commerce websites and an increase in dollar value per transaction. This was partially offset by an increase in selling, general and administrative expenses including higher digital marketing expenses and higher variable costs such as distribution costs, credit card fees, and packaging as a result of higher net revenue. Income from operations as a percentage of direct to consumer revenue decreased by 200 basis points, primarily due to deleverage of selling, general and administrative expenses, partially offset by an increase in gross margin.

Other. Other income from operations increase d \$3.9 million , or 140% , to \$6.7 million for the first two quarters of fiscal 2016 from \$2.8 million for the first two quarters of fiscal 2015 . The increase was primarily the result of increase d gross profit of \$11.3 million , partially offset by increased selling, general and administrative expenses primarily due to increased employee costs. Income from operations as a percentage of other net revenue increased by 300 basis points, primarily due to decreased selling, general and administrative expenses as a percentage of other net revenue.

General Corporate Expense. General corporate expense increased \$27.9 million , or 39% , to \$99.9 million for the first two quarters of fiscal 2016 from \$72.0 million for the first two quarters of fiscal 2015 . This was primarily due to increased employee costs, professional fees, including increased professional fees related to supply chain consulting, investment in strategic initiatives and projects to support the growth of our business, and due to an increase in net foreign exchange losses of \$9.6 million , primarily related to the revaluation of U.S. dollar cash and receivables held in Canada.

Other Income (Expense), Net

Other income (expense), net decrease d \$1.3 million , or 93% , to \$0.1 million in the first two quarters of fiscal 2016 from \$1.4 million in the first two quarters of fiscal 2015 . The decrease was primarily due to net interest expenses of \$1.5 million related to certain tax adjustments that are outlined in Note 7 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report.

Income Tax Expense

Income tax expense decreased \$7.8 million , or 19% , to \$32.7 million in the first two quarters of fiscal 2016 from \$40.5 million in the first two quarters of fiscal 2015 . The first two quarters of fiscal 2016 included certain tax adjustments totaling a

recovery of \$7.6 million as outlined in Note 7 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report.

The effective tax rate in the first two quarters of fiscal 2016 was 24.8% compared to 29.8% in the first two quarters of fiscal 2015 . The effective tax rate excluding the above tax and related interest adjustments was 30.2% in the first two quarters of fiscal 2016 .

Net Income

Net income increased \$3.5 million , or 4% , to \$99.0 million for the first two quarters of fiscal 2016 from \$95.5 million for the first two quarters of fiscal 2015 . The increase in net income was primarily a result of an increase in gross profit of \$75.4 million and a decrease in income tax expense of \$7.8 million , partially offset by an increase in selling, general and administrative expenses of \$78.5 million and a decrease in other income (expense), net of \$1.3 million .

Comparable Store Sales and Total Comparable Sales

We separately track comparable store sales, which reflect net revenue from company-operated stores that have been open for at least 12 months, or open for at least 12 months after being significantly expanded. Net revenue from a store is included in comparable store sales beginning with the first month for which the store has a full month of comparable sales in the prior year. Comparable store sales exclude sales from new stores that have not been open for 12 months, from stores which have not been in their significantly expanded space for 12 months, and from stores which have been temporarily relocated for renovations. Comparable stores sales also exclude sales from direct to consumer, outlets, showrooms, wholesale accounts, warehouse sales, temporary locations, a license and supply arrangement, and sales from company-operated stores which we have closed.

Total comparable sales combines comparable store sales and direct to consumer sales. By measuring the change in year-over-year net revenue in stores that have been open, or in their significantly expanded space, for 12 months or more as well as the change in direct to consumer sales, total comparable sales allows us to evaluate our sales performance eliminating the impact of newly opened or expanded stores.

Non-GAAP Financial Measures

Constant dollar changes in net revenue, total comparable sales, comparable store sales, and direct to consumer net revenue, and the effective tax rate and diluted earnings per share excluding certain tax and related interest adjustments, are non-GAAP financial measures.

A constant dollar basis assumes the average foreign exchange rates for the current period remained constant with the average foreign exchange rates for the same period of the prior year. We provide constant dollar changes in net revenue, total comparable sales, comparable store sales, and changes in direct to consumer net revenue because we use these measures to understand the underlying growth rate of net revenue excluding the impact of changes in foreign exchange rates, which are not under management's control. We believe that disclosing these measures on a constant dollar basis is useful to investors because it enables them to better understand the level of growth of our business.

We disclose the effective tax rate and diluted earnings per share excluding certain tax and related interest adjustments because of their comparability to our historical information, which we believe is useful to investors.

The presentation of this financial information is not intended to be considered in isolation or as a substitute for, or with greater prominence to, the financial information prepared and presented in accordance with GAAP. A reconciliation of the non-GAAP financial measures follows, which includes more detail on the GAAP financial measure that is most directly comparable to each non-GAAP financial measure, and the related reconciliations between these financial measures.

The below changes in net revenue, total comparable sales, comparable store sales, and direct to consumer revenue show the change compared to the corresponding period in the prior year.

Constant dollar changes in net revenue

	Thirteen Weeks Ended July 31, 2016 and August 2, 2015			
	2016		2015	
	<i>(In thousands)</i>		<i>(Percentages)</i>	
Net revenue increase	\$ 61,510	\$ 62,302	14%	16%
Adjustments due to foreign exchange rate changes	5,251	20,293	1	5
Net revenue increase in constant dollars	\$ 66,761	\$ 82,595	15%	21%

	Twenty-Six Weeks Ended July 31, 2016 and August 2, 2015			
	2016		2015	
	<i>(In thousands)</i>		<i>(Percentages)</i>	
Net revenue increase	\$ 133,483	\$ 101,228	15%	13%
Adjustments due to foreign exchange rate changes	12,542	35,788	2	5
Net revenue increase in constant dollars	\$ 146,025	\$ 137,016	17%	18%

Constant dollar changes in total comparable sales

	Thirteen Weeks Ended July 31, 2016 and August 2, 2015		Twenty-Six Weeks Ended July 31, 2016 and August 2, 2015	
	2016	2015	2016	2015
	<i>(Percentages)</i>			
Increase in total comparable sales ¹	4%	6%	5%	4%
Adjustments due to foreign exchange rate changes	1	5	1	4
Increase in total comparable sales in constant dollars ¹	5%	11%	6%	8%

¹ Total comparable sales includes comparable store sales and direct to consumer sales. Comparable store sales reflects net revenue from company-operated stores that have been open for at least 12 months, or open for at least 12 months after being significantly expanded.

Constant dollar changes in comparable store sales

	Thirteen Weeks Ended July 31, 2016 and August 2, 2015			
	2016		2015	
	<i>(In thousands)</i>		<i>(Percentages)</i>	
Increase in comparable store sales ¹	\$ 10,416	\$ 1,390	3%	1%
Adjustments due to foreign exchange rate changes	3,171	12,833	1	5
Increase in comparable store sales in constant dollars ¹	\$ 13,587	\$ 14,223	4%	6%

	Twenty-Six Weeks Ended July 31, 2016 and August 2, 2015			
	2016		2015	
	<i>(In thousands)</i>		<i>(Percentages)</i>	
Increase (decrease) in comparable store sales ¹	\$ 18,933	\$ (10,748)	3%	(2)%
Adjustments due to foreign exchange rate changes	7,681	22,531	1	4
Increase in comparable store sales in constant dollars ¹	\$ 26,614	\$ 11,783	4%	2%

¹ Comparable store sales reflects net revenue from company-operated stores that have been open for at least 12 months, or open for at least 12 months after being significantly expanded.

Constant dollar changes in direct to consumer net revenue

	Thirteen Weeks Ended July 31, 2016 and August 2, 2015		Twenty-Six Weeks Ended July 31, 2016 and August 2, 2015	
	2016	2015	2016	2015
	<i>(Percentages)</i>			
Increase in direct to consumer net revenue	6%	30%	12%	28%
Adjustments due to foreign exchange rate changes	1	5	1	5
Increase in direct to consumer net revenue in constant dollars	7%	35%	13%	33%

Effective tax rate, excluding tax and related interest adjustments

	Thirteen Weeks Ended July 31, 2016 and August 2, 2015		Twenty-Six Weeks Ended July 31, 2016 and August 2, 2015	
	2016	2015	2016	2015
	<i>(Percentages)</i>			
Effective tax rate	28.1%	29.3%	24.8%	29.8%
Tax and related interest adjustments ¹	2.4	—	5.4	—
Effective tax rate, excluding tax and related interest adjustments	30.5%	29.3%	30.2%	29.8%

¹ Please refer to Note 7 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report for an explanation as to the nature of these items.

Diluted earnings per share, excluding tax and related interest adjustments

	Thirteen Weeks Ended July 31, 2016 and August 2, 2015		Twenty-Six Weeks Ended July 31, 2016 and August 2, 2015	
	2016	2015	2016	2015
Diluted earnings per share	\$ 0.39	\$ 0.34	\$ 0.72	\$ 0.67
Tax and related interest adjustments ¹	(0.01)	—	(0.04)	—
Diluted earnings per share, excluding tax and related interest adjustments	\$ 0.38	\$ 0.34	\$ 0.68	\$ 0.67

¹ Please refer to Note 7 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report for an explanation as to the nature of these items.

Seasonality

Our business is affected by the general seasonal trends common to the retail apparel industry. Our annual net revenue is weighted more heavily toward our fourth fiscal quarter, reflecting our historical strength in sales during the holiday season, while our operating expenses are more equally distributed throughout the year. As a result, a substantial portion of our operating profits are generated in the fourth quarter of our fiscal year.

Liquidity and Capital Resources

Our primary sources of liquidity are our current balances of cash and cash equivalents and cash flows from operations. Our primary cash needs are capital expenditures for opening new stores and remodeling or relocating existing stores, making information technology system enhancements, funding working capital requirements, and making other strategic capital investments both in North America and internationally. We may also use cash to repurchase shares of our common stock. Cash and cash equivalents in excess of our needs are held in interest bearing accounts with financial institutions.

At July 31, 2016, our working capital (excluding cash and cash equivalents) was \$229.9 million and our cash and cash equivalents were \$535.3 million.

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

	Twenty-Six Weeks Ended July 31, 2016 and August 2, 2015	
	2016	2015
<i>(In thousands)</i>		
Total cash provided by (used in):		
Operating activities	\$ 99,988	\$ 32,161
Investing activities	(71,261)	(65,118)
Financing activities	(23,877)	(78,837)
Effect of exchange rate changes on cash	29,018	(11,423)
Increase (decrease) in cash and cash equivalents	<u>\$ 33,868</u>	<u>\$ (123,217)</u>

Operating Activities

Cash flows provided by operating activities consist primarily of net income adjusted for certain items not affecting cash and the effect of changes in operating assets and liabilities.

Cash provided by operating activities increased \$67.8 million, to \$100.0 million for the first two quarters of fiscal 2016 compared to \$32.2 million for the first two quarters of fiscal 2015. The increase was primarily the result of decreased inventory purchases and an increase in net income taxes payable.

Investing Activities

Cash flows used in investing activities relate entirely to capital expenditures. The capital expenditures were primarily for opening new company-operated stores, remodeling or relocating certain stores, and ongoing store refurbishment. We also had capital expenditures related to information technology and business systems, related to corporate land and buildings, and for opening retail locations other than company-operated stores.

Cash used in investing activities increased \$6.1 million to \$71.3 million for the first two quarters of fiscal 2016 from \$65.1 million for the first two quarters of fiscal 2015. The increase was primarily the result of the purchase of a land parcel in Vancouver, BC for \$19.7 million for general corporate purposes. The increase was partially offset by reduced capital expenditures related to our company-operated stores primarily as a result of opening fewer company-operated stores in the first two quarters of fiscal 2016 compared to the first two quarters of fiscal 2015.

Financing Activities

Cash flows used in or provided by financing activities consist primarily of cash used to repurchase shares of our common stock and certain cash flows related to stock-based compensation.

Cash used in financing activities decreased \$55.0 million, to \$23.9 million for the first two quarters of fiscal 2016 compared to \$78.8 million for the first two quarters of fiscal 2015. Our cash used in financing activities for the first two quarters of fiscal 2016 included \$28.6 million to repurchase 0.4 million shares under our stock repurchase program compared to \$82.0 million to repurchase 1.3 million shares for the first two quarters of fiscal 2015.

We believe that our cash and cash equivalent balances, cash generated from operations, and borrowings available to us under our revolving credit facility will be adequate to meet our liquidity needs and capital expenditure requirements for at least the next 12 months. Our cash from operations may be negatively impacted by a decrease in demand for our products as well as the other factors described in Item 1 of Part II of this Quarterly Report on Form 10-Q. In addition, we may make discretionary capital improvements with respect to our stores, distribution facilities, headquarters, or systems, which we would expect to fund through the use of cash, issuance of debt or equity securities or other external financing sources to the extent we were unable to fund such capital expenditures out of our cash and cash equivalents and cash generated from operations.

Revolving Credit Facility

In November 2013, we entered into unsecured demand revolving credit facilities with HSBC Bank Canada and Bank of America, N.A., Canada Branch, for up to \$15.0 million in the aggregate to support the issuance of letters of credit and to fund our working capital requirements. Borrowings under the uncommitted credit facilities are made on a when-and-as-needed basis at our discretion. These facilities were renewed for a one year period in November 2015.

Borrowings under the credit facility can be made either as (i) U.S. Dollar Loans - U.S. Dollar Loans bear interest a rate equal to U.S. LIBOR plus 100 basis points or U.S. Base Rate, at our option; (ii) Letters of Credit - Borrowings drawn down under standby letters of credit issued by the banks bear a fee of 100 basis points; and (iii) CDN Dollar Loans - CDN Dollar Loans bear interest at a rate equal to the CDOR Rate plus 100 basis points or the Canadian Prime Rate, at our option.

At July 31, 2016, aside from letters of credit, there were no borrowings outstanding under these credit facilities.

Off-Balance Sheet Arrangements

We enter into standby letters of credit to secure certain of our obligations, including leases, taxes and duties. As of July 31, 2016, letters of credit and letters of guarantee totaling \$1.5 million had been issued.

We have not entered into any transactions, agreements or other contractual arrangements to which an entity unconsolidated with us is a party and under which we have (i) any obligation under a guarantee, (ii) any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity, (iii) any obligation under derivative instruments that are indexed to our shares and classified as equity in our consolidated balance sheets, or (iv) any obligation arising out of a variable interest in any unconsolidated entity that provides financing, liquidity, market risk or credit support to us or engages in leasing, hedging or research and development services with us.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions. Predicting future events is inherently an imprecise activity and, as such, requires the use of judgment. Actual results may vary from our estimates in amounts that may be material to the financial statements. An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, and if different estimates that reasonably could have been used or changes in the accounting estimates that are reasonably likely to occur periodically, could materially impact our consolidated financial statements. Our critical accounting policies and estimates are discussed in our Annual Report on Form 10-K for our 2015 fiscal year end filed with the SEC on March 30, 2016 and in Note 2 included in Item 1 of Part I of this Quarterly Report on Form 10-Q.

Operating Locations

Our company-operated stores by brand and by country as of July 31, 2016 and January 31, 2016 , are summarized in the table below.

	July 31, 2016	January 31, 2016
lululemon athletica		
United States	231	229
Canada	49	48
Australia	27	26
United Kingdom	6	6
New Zealand	5	5
Singapore	3	2
Hong Kong	2	2
Germany	1	1
Puerto Rico	1	1
South Korea	1	—
Switzerland	1	—
	327	320
ivivva athletica		
United States	39	31
Canada	13	12
	52	43
Total	379	363

As of July 31, 2016 , there were three retail locations in the United Arab Emirates operated by a third party under a license and supply arrangement, which are not included in the above table.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

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

Foreign Currency Exchange Risk . The functional currency of our foreign subsidiaries is generally the applicable local currency. Our consolidated financial statements are presented in U.S. dollars. Therefore, the net revenue, expenses, assets, and liabilities of our foreign subsidiaries are translated from their functional currencies into U.S. dollars. Fluctuations in the value of the U.S. dollar affect the reported amounts of net revenue, expenses, assets, and liabilities. Foreign exchange differences which arise on translation of our foreign subsidiaries' balance sheets into U.S. dollars are recorded as a foreign currency translation adjustment in accumulated other comprehensive income or loss within stockholders' equity.

We also have exposure to changes in foreign exchange rates associated with transactions which are undertaken by our subsidiaries in currencies other than their functional currency. Such transactions include intercompany transactions and inventory purchases denominated in currencies other than the functional currency of the purchasing entity. As a result, we have been impacted by changes in exchange rates and may be impacted materially for the foreseeable future. The potential impact of currency fluctuation increases as international expansion increases.

We currently generate a significant portion of our net revenue and incur a significant portion of our expenses in Canada. We also hold a significant portion of our net assets in Canada. The reporting currency for our consolidated financial statements is the U.S. dollar. A strengthening of the U.S. dollar against the Canadian dollar results in:

- a decrease in our net revenue upon translation of the sales made by our Canadian operations into U.S. dollars for the purposes of consolidation;
- a decrease in our selling, general and administrative expenses incurred by our Canadian operations upon translation into U.S. dollars for the purposes of consolidation; and

- foreign exchange revaluation gains by our Canadian subsidiaries on U.S. dollar cash and receivables denominated in U.S. dollars.

During the first two quarters of fiscal 2016 , the change in the relative value of the U.S. dollar against the Canadian dollar resulted in a \$44.0 million reduction in accumulated other comprehensive loss within stockholders' equity. During the first two quarters of fiscal 2015 , the change in the relative value of the U.S. dollar against the Canadian dollar resulted in a \$18.0 million increase in accumulated other comprehensive loss within stockholders' equity.

A 10% appreciation in the relative value of the U.S. dollar against the Canadian dollar compared to the exchange rates in effect for the first two quarters of fiscal 2016 would have resulted in additional income from operations of approximately \$5.4 million in the first two quarters of fiscal 2016 . This assumes a consistent 10% appreciation in the U.S. dollar against the Canadian dollar throughout the first two quarters of fiscal 2016 . The timing of changes in the relative value of the U.S. dollar combined with the seasonal nature of our business, can affect the magnitude of the impact that fluctuations in foreign exchange rates have on our income from operations.

We have not historically hedged foreign currency fluctuations. However, in the future, in an effort to mitigate losses associated with these risks, we may at times enter into derivative financial instruments, although we have not historically done so. We do not, and do not intend to, engage in the practice of trading derivative securities for profit.

Interest Rate Risk . Our revolving credit facilities provide us with available borrowings in an amount up to \$15.0 million in the aggregate. Because our revolving credit facilities bear interest at a variable rate, we will be exposed to market risks relating to changes in interest rates, if we have a meaningful outstanding balance. As of July 31, 2016 , aside from letters of credit, we had no outstanding balances under our revolving facilities. We currently do not engage in any interest rate hedging activity and currently have no intention to do so in the foreseeable future. However, in the future, if we have a meaningful outstanding balance under our revolving facility, in an effort to mitigate losses associated with these risks, we may at times enter into derivative financial instruments, although we have not historically done so. These may take the form of forward contracts, option contracts, or interest rate swaps. We do not, and do not intend to, engage in the practice of trading derivative securities for profit.

Inflation

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

ITEM 4. CONTROLS AND PROCEDURES

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed by us in the reports we file or submit under the Securities Exchange Act of 1934, or the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer (principal executive officer) and Chief Financial Officer (principal financial officer), to allow timely decisions to be made regarding required disclosure. We have established a Disclosure Committee, consisting of certain members of management, to assist in this evaluation. The Disclosure Committee meets on a quarterly basis, and as needed.

Our management, including our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Exchange Act), at July 31, 2016 . Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, at July 31, 2016 , our disclosure controls and procedures were effective.

There were no changes in our internal control over financial reporting during the thirteen weeks ended July 31, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In addition to the legal matters described in Note 6 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report and in our fiscal 2015 Annual Report on Form 10-K, we are, from time to time, involved in routine legal matters incidental to the conduct of our business, including legal matters such as initiation and defense of proceedings to protect intellectual property rights, personal injury claims, product liability claims, and similar matters. We believe the ultimate resolution of any such current proceeding will not have a material adverse effect on our continued financial position, results of operations or cash flows.

ITEM 1A. RISK FACTORS

In addition to the other information contained in this Form 10-Q and in our Annual Report on Form 10-K for our 2015 fiscal year, the following risk factors should be considered carefully in evaluating our business. Our business, financial condition or results of operations could be materially adversely affected by any of these risks. Please note that additional risks not presently known to us or that we currently deem immaterial could also impair our business and operations.

Our success depends on our ability to maintain the value and reputation of our brand.

Our success depends on the value and reputation of the lululemon athletica brand. The lululemon athletica name is integral to our business as well as to the implementation of our strategies for expanding our business. Maintaining, promoting, and positioning our brand will depend largely on the success of our marketing and merchandising efforts and our ability to provide a consistent, high quality product, and guest experience. We rely on social media, as one of our marketing strategies, to have a positive impact on both our brand value and reputation. Our brand and reputation could be adversely affected if we fail to achieve these objectives, if our public image was to be tarnished by negative publicity, if we fail to deliver innovative and high quality products acceptable to our guests, or if we face a product recall. Negative publicity regarding the production methods of any of our suppliers or manufacturers could adversely affect our reputation and sales and force us to locate alternative suppliers or manufacturing sources. Additionally, while we devote considerable efforts and resources to protecting our intellectual property, if these efforts are not successful the value of our brand may be harmed. Any harm to our brand and reputation could have a material adverse effect on our financial condition.

If any of our products are unacceptable to us or our guests, our business could be harmed.

We have occasionally received, and may in the future continue to receive, shipments of products that fail to comply with our technical specifications or that fail to conform to our quality control standards. We have also received, and may in the future continue to receive, products that either meet our technical specifications but that are nonetheless unacceptable to us, or products that are otherwise unacceptable to us or our guests. Under these circumstances, unless we are able to obtain replacement products in a timely manner, we risk the loss of net revenue resulting from the inability to sell those products and related increased administrative and shipping costs. Additionally, if the unacceptability of our products are not discovered until after such products are purchased by our guests, our guests could lose confidence in the technical attributes of our products or we could face a product recall and our results of operations could suffer and our business, reputation, and brand could be harmed.

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

The market for technical athletic apparel is highly competitive. Competition may result in pricing pressures, reduced profit margins or lost market share, or a failure to grow or maintain our market share, any of which could substantially harm our business and results of operations. We compete directly against wholesalers and direct retailers of athletic apparel, including large, diversified apparel companies with substantial market share and established companies expanding their production and marketing of technical athletic apparel, as well as against retailers specifically focused on women's athletic apparel. We also face competition from wholesalers and direct retailers of traditional commodity athletic apparel, such as cotton T-shirts and sweatshirts. Many of our competitors are large apparel and sporting goods companies with strong worldwide brand recognition. Because of the fragmented nature of the industry, we also compete with other apparel sellers, including those specializing in yoga apparel and other activewear. Many of our competitors have significant competitive advantages, including longer operating histories, larger and broader customer bases, more established relationships with a broader set of suppliers, greater brand recognition and greater financial, research and development, store development, marketing, distribution, and other resources than we do. In addition, our technical athletic apparel is sold at a price premium to traditional athletic apparel.

Our competitors may be able to achieve and maintain brand awareness and market share more quickly and effectively than we can. In contrast to our "grassroots" marketing approach, many of our competitors promote their brands through traditional forms of advertising, such as print media and television commercials, and through celebrity endorsements, and have substantial resources to devote to such efforts. Our competitors may also create and maintain brand awareness using traditional forms of advertising more quickly than we can. Our competitors may also be able to increase sales in their new and existing markets faster than we do by emphasizing different distribution channels than we do, such as catalog sales or an extensive franchise network, as opposed to distribution through retail stores, wholesale or internet, and many of our competitors have substantial resources to devote toward increasing sales in such ways.

In addition, because we hold limited patents and exclusive intellectual property rights in the technology, fabrics or processes underlying our products, our current and future competitors are able to manufacture and sell products with performance characteristics, fabrication techniques, and styling similar to our products.

Our reliance on suppliers to provide fabrics for and to produce our products could cause problems in our supply chain.

We do not manufacture our products or the raw materials for them and rely instead on suppliers. Many of the specialty fabrics used in our products are technically advanced textile products developed and manufactured by third parties and may be available, in the short-term, from only one or a very limited number of sources. For example, Luon fabric, which is included in many of our products, is supplied to the garment factories we use by a limited number of manufacturers, and the components used in manufacturing Luon fabric may each be supplied to our manufacturers by single companies. In fiscal 2015, approximately 65% of our products were produced by our top five manufacturing suppliers, 40% of raw materials were produced by a single manufacturer. We have no long-term contracts with any of our suppliers or manufacturing sources for the production and supply of our fabrics and garments, and we compete with other companies for fabrics, raw materials, and production.

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

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

Many of our products may be considered discretionary items for consumers. Factors affecting the level of consumer spending for such discretionary items include general economic conditions, particularly those in North America and other factors such as consumer confidence in future economic conditions, fears of recession, the availability and cost of consumer credit, levels of unemployment, and tax rates. As global economic conditions continue to be volatile or economic uncertainty remains, trends in consumer discretionary spending also remain unpredictable and subject to reductions due to credit constraints and uncertainties about the future. Unfavorable economic conditions may lead consumers to delay or reduce purchases of our products. Consumer demand for our products may not reach our targets, or may decline, when there is an economic downturn or economic uncertainty in our key markets, particularly in North America. Our sensitivity to economic cycles and any related fluctuation in consumer demand may have a material adverse effect on our financial condition.

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

Our business is subject to significant pressure on costs and pricing caused by many factors, including intense competition, constrained sourcing capacity and related inflationary pressure, pressure from consumers to reduce the prices we charge for our products, and changes in consumer demand. These factors may cause us to experience increased costs, reduce our prices to consumers or experience reduced sales in response to increased prices, any of which could cause our operating

margin to decline if we are unable to offset these factors with reductions in operating costs and could have a material adverse effect on our financial conditions, operating results and cash flows.

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

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

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

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

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

Our inability to safeguard against security breaches with respect to our information technology systems could disrupt our operations.

Our business employs systems and websites that allow for the storage and transmission of proprietary or confidential information regarding our business, guests and employees including credit card information. Security breaches could expose us to a risk of loss or misuse of this information and potential liability. We may not have the resources or technical sophistication to be able to anticipate or prevent rapidly evolving types of cyber-attacks. Actual or anticipated attacks may cause us to incur increasing costs including costs to deploy additional personnel and protection technologies, train employees and engage third party experts and consultants. Advances in computer capabilities, new technological discoveries or other developments may result in the technology used by us to protect transaction or other data being breached or compromised. Data and security breaches can also occur as a result of non-technical issues including intentional or inadvertent breach by employees or persons with whom we have commercial relationships that result in the unauthorized release of personal or confidential information. Any compromise or breach of our security could result in a violation of applicable privacy and other laws, significant litigation and potential liability and damage to our brand and reputation or other harm to our business.

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

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

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

We have expanded our operations rapidly since our inception in 1998 and our net revenue has increased from \$40.7 million in fiscal 2004 to \$2.1 billion in fiscal 2015. If our operations continue to grow at a rapid pace, we may experience difficulties in obtaining sufficient raw materials and manufacturing capacity to produce our products, as well as delays in production and shipments, as our products are subject to risks associated with overseas sourcing and manufacturing. We could be required to continue to expand our sales and marketing, product development and distribution functions, to upgrade our management information systems and other processes and technology, and to obtain more space for our expanding workforce. This expansion could increase the strain on our resources, and we could experience operating difficulties, including difficulties in hiring, training and managing an increasing number of employees. These difficulties could result in the erosion of our brand image which could have a material adverse effect on our financial condition.

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

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

Our limited operating experience and limited brand recognition in new international markets may limit our expansion strategy and cause our business and growth to suffer.

Our future growth depends in part on our expansion efforts outside of North America. We have limited experience with regulatory environments and market practices internationally, and we may not be able to penetrate or successfully operate in any new market. In connection with our expansion efforts we may encounter obstacles we did not face in North America, including cultural and linguistic differences, differences in regulatory environments, labor practices and market practices, difficulties in keeping abreast of market, business and technical developments, and foreign guests' tastes and preferences. We may also encounter difficulty expanding into new international markets because of limited brand recognition leading to delayed acceptance of our technical athletic apparel by guests in these new international markets. Our failure to develop our business in new international markets or experiencing disappointing growth outside of existing markets could harm our business and results of operations.

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

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

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

The intellectual property rights in the technology, fabrics, and processes used to manufacture our products generally are owned or controlled by our suppliers and are generally not unique to us. Our ability to obtain intellectual property protection for our products is therefore limited and we do not generally own patents or hold exclusive intellectual property rights in the technology, fabrics or processes underlying our products. As a result, our current and future competitors are able to manufacture and sell products with performance characteristics, fabrics and styling similar to our products. Because many of our competitors have significantly greater financial, distribution, marketing, and other resources than we do, they may be able to manufacture and sell products based on our fabrics and manufacturing technology at lower prices than we can. If our competitors do sell similar products to ours at lower prices, our net revenue and profitability could suffer.

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

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

Changes in tax laws or unanticipated tax liabilities could adversely affect our effective income tax rate and profitability.

We are subject to the income tax laws of the United States, Canada, and several other international jurisdictions. Our effective income tax rates could be unfavorably impacted by a number of factors, including changes in the mix of earnings amongst countries with differing statutory tax rates, changes in the valuation of deferred tax assets and liabilities, changes in tax laws, the outcome of income tax audits in various jurisdictions around the world, and any repatriation of unremitted earnings for which we have not previously accrued U.S. taxes.

We and our subsidiaries engage in a number of intercompany transactions across multiple tax jurisdictions. Although we believe that these transactions reflect the accurate economic allocation of profit and that proper transfer pricing documentation is in place, the profit allocation and transfer pricing terms and conditions may be scrutinized by local tax authorities during an audit and any resulting changes may impact our mix of earnings in countries with differing statutory tax rates.

Current economic and political conditions make tax rules in any jurisdiction, including the United States and Canada, subject to significant change. There have been proposals to reform U.S. and foreign tax laws that could significantly impact how U.S. multinational corporations are taxed on foreign earnings. Although we cannot predict whether or in what form such proposals will pass, several of the proposals considered, if enacted into law, could have an adverse impact on our income tax expense and cash flows.

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

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

We also lease the majority of our distribution centers and our inability to secure appropriate real estate or lease terms could impact our ability to deliver our products to the market.

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

A significant portion of our products are produced in South and South East Asia and increases in the costs of labor and other costs of doing business in the countries in this area could significantly increase our costs to produce our products and could have a negative impact on our operations, net revenue, and earnings. Factors that could negatively affect our business include a potential significant revaluation of the currencies used in these countries, which may result in an increase in the cost of producing products, labor shortage and increases in labor costs, and difficulties in moving products manufactured out of the countries in which they are manufactured and through the ports on the western coast of North America, whether due to port congestion, labor disputes, product regulations and/or inspections or other factors, and natural disasters or health pandemics. A labor strike or other transportation disruption affecting these ports could significantly disrupt our business. Also, the imposition of trade sanctions or other regulations against products imported by us from, or the loss of "normal trade relations" status with any country in which our products are manufactured, could significantly increase our cost of products imported into North America and/or Australia and harm our business.

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

Our growth will largely depend on our ability to successfully open and operate new stores, which depends on many factors, including, among others, our ability to:

- identify suitable store locations, the availability of which is outside of our control;
- negotiate acceptable lease terms, including desired tenant improvement allowances;
- hire, train and retain store personnel and field management;
- immerse new store personnel and field management into our corporate culture;
- source sufficient inventory levels; and
- successfully integrate new stores into our existing operations and information technology systems.

Successful new store openings may also be affected by our ability to initiate our grassroots marketing efforts in advance of opening our first store in a new market. We typically rely on our grassroots marketing efforts to build awareness of our brand and demand for our products. Our grassroots marketing efforts are often lengthy and must be tailored to each new market based on our emerging understanding of the market. We may not be able to successfully implement our grassroots marketing efforts in a particular market in a timely manner, if at all. Additionally, we may be unsuccessful in identifying new markets where our technical athletic apparel and other products and brand image will be accepted or the performance of our stores will be considered successful.

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

The labeling, distribution, importation, marketing, and sale of our products are subject to extensive regulation by various federal agencies, including the Federal Trade Commission, Consumer Product Safety Commission and state attorneys general in the United States, the Competition Bureau and Health Canada in Canada, as well as by various other federal, state, provincial, local and international regulatory authorities in the countries in which our products are distributed or sold. If we fail to comply with any of these regulations, we could become subject to enforcement actions or the imposition of significant penalties or claims, which could harm our results of operations or our ability to conduct our business. In addition, the adoption of new regulations or changes in the interpretation of existing regulations may result in significant compliance costs or discontinuation of product sales and could impair the marketing of our products, resulting in significant loss of net revenue.

Our international operations are also subject to compliance with the U.S. Foreign Corrupt Practices Act, or FCPA, and other anti-bribery laws applicable to our operations. In many foreign countries, particularly in those with developing economies, it may be a local custom that businesses operating in such countries engage in business practices that are prohibited by the FCPA or other U.S. and foreign laws and regulations applicable to us. Although we have implemented procedures designed to ensure compliance with the FCPA and similar laws, some of our employees, agents, or other channel partners, as well as those companies to which we outsource certain of our business operations, could take actions in violation of our policies. Any such violation could have a material and adverse effect on our business.

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

Our future success is substantially dependent on the continued service of our senior management and other key employees. In the last several years, several members of our senior management team have left us and we have focused time and resources on recruiting the new members of our current management team. The continued turnover of senior management and the loss of key members of our executive team could have a negative impact on our ability to manage and grow our business effectively. In addition, if we're not effective with our succession planning, it may have a negative impact on our ability to fill senior management roles in a timely manner.

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

Our business is affected by seasonality.

Our business is affected by the general seasonal trends common to the retail apparel industry. Our annual net revenue is weighted more heavily toward our fourth fiscal quarter, reflecting our historical strength in sales during the holiday season, while our operating expenses are more equally distributed throughout the year. As a result, a substantial portion of our

operating profits are generated in the fourth quarter of our fiscal year. For example, we generated approximately 45%, 42% and 39% of our full year operating profit during the fourth quarters of fiscal 2015, fiscal 2014 and fiscal 2013, respectively. This seasonality may adversely affect our business and cause our results of operations to fluctuate, and, as a result, we believe that comparisons of our operating results between different quarters within a single fiscal year are not necessarily meaningful and that results of operations in any period should not be considered indicative of the results to be expected for any future period.

Because a significant portion of our net revenue and expenses are generated in countries other than the United States, fluctuations in foreign currency exchange rates have affected our results of operations and may continue to do so in the future.

The functional currency of our foreign subsidiaries is generally the applicable local currency. Our consolidated financial statements are presented in U.S. dollars. Therefore, the net revenue, expenses, assets, and liabilities of our foreign subsidiaries are translated from their functional currencies into U.S. dollars. Fluctuations in the value of the U.S. dollar affect the reported amounts of net revenue, expenses, assets, and liabilities. Foreign exchange differences which arise on translation of our foreign subsidiaries' balance sheets into U.S. dollars are recorded as a foreign currency translation adjustment in accumulated other comprehensive income or loss within stockholders' equity. We also have exposure to changes in foreign exchange rates associated with transactions which are undertaken by our subsidiaries in currencies other than their functional currency. Such transactions include intercompany transactions and inventory purchases denominated in currencies other than the functional currency of the purchasing entity. As a result, we have been impacted by changes in exchange rates and may be impacted materially for the foreseeable future. The potential impact of currency fluctuation increases as international expansion increases.

We currently generate a significant portion of our net revenue and incur a significant portion of our expenses in Canada. We also hold a significant portion of our net assets in Canada. The reporting currency for our consolidated financial statements is the U.S. dollar. A strengthening of the U.S. dollar against the Canadian dollar results in:

- a decrease in our net revenue upon translation of the sales made by our Canadian operations into U.S. dollars for the purposes of consolidation;
- a decrease in our selling, general and administrative expenses incurred by our Canadian operations upon translation into U.S. dollars for the purposes of consolidation; and
- foreign exchange revaluation gains by our Canadian subsidiaries on U.S. dollar cash and receivables denominated in U.S. dollars.

During the first two quarters of fiscal 2016, the change in the relative value of the U.S. dollar against the Canadian dollar resulted in a \$44.0 million reduction in accumulated other comprehensive loss within stockholders' equity. During the first two quarters of fiscal 2015, the change in the relative value of the U.S. dollar against the Canadian dollar resulted in a \$18.0 million increase in accumulated other comprehensive loss within stockholders' equity.

A 10% appreciation in the relative value of the U.S. dollar against the Canadian dollar compared to the exchange rates in effect for the first two quarters of fiscal 2016 would have resulted in additional income from operations of approximately \$5.4 million in the first two quarters of fiscal 2016. This assumes a consistent 10% appreciation in the U.S. dollar against the Canadian dollar throughout the first two quarters of fiscal 2016. The timing of changes in the relative value of the U.S. dollar combined with the seasonal nature of our business, can affect the magnitude of the impact that fluctuations in foreign exchange rates have on our income from operations.

We have not historically hedged foreign currency fluctuations. However, in the future, in an effort to mitigate losses associated with these risks, we may at times enter into derivative financial instruments, although we have not historically done so. We do not, and do not intend to, engage in the practice of trading derivative securities for profit.

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

Almost all of our suppliers are located outside of North America. During fiscal 2015, approximately 44% of our products were produced in South East Asia, approximately 28% in South Asia, approximately 20% in China, approximately 2% in North America, and the remainder in other regions. As a result of our international suppliers, we are subject to risks associated with doing business abroad, including:

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

- the imposition of new laws and regulations, including those relating to labor conditions, quality and safety standards, imports, duties, taxes and other charges on imports, as well as trade restrictions and restrictions on currency exchange or the transfer of funds;
- reduced protection for intellectual property rights, including trademark protection, in some countries, particularly China;
- disruptions or delays in shipments; and
- changes in local economic conditions in countries where our manufacturers, suppliers, or guests are located.

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

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

The United States and the countries in which our products are produced or sold internationally have imposed and may impose additional quotas, duties, tariffs, or other restrictions or regulations, or may adversely adjust prevailing quota, duty or tariff levels. We have expanded our relationships with suppliers outside of China, which among other things has resulted in increased costs and shipping times for some products. Countries impose, modify and remove tariffs and other trade restrictions in response to a diverse array of factors, including global and national economic and political conditions, which make it impossible for us to predict future developments regarding tariffs and other trade restrictions. Trade restrictions, including tariffs, quotas, embargoes, safeguards, and customs restrictions, could increase the cost or reduce the supply of products available to us or may require us to modify our supply chain organization or other current business practices, any of which could harm our business, financial condition and results of operations.

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

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

We are subject to periodic claims and litigation that could result in unexpected expenses and could ultimately be resolved against us.

From time to time, we are involved in litigation and other proceedings, including matters related to product liability claims, stockholder class action and derivative claims, commercial disputes and intellectual property, as well as trade, regulatory, and other claims related to our business. Any of these proceedings could result in significant settlement amounts, damages, fines or other penalties, divert financial and management resources, and result in significant legal fees. An unfavorable outcome of any particular proceeding could exceed the limits of our insurance policies or the carriers may decline to fund such final settlements and/or judgments and could have an adverse impact on our business, financial condition, and results of operations. In addition, any proceeding could negatively impact our reputation among our guests and our brand image.

Our business could be negatively affected as a result of actions of activist stockholders, and such activism could impact the trading value of our securities.

Responding to actions by activist stockholders can be costly and time-consuming, disrupting our operations and diverting the attention of management and our employees. Such activities could interfere with our ability to execute our strategic plan. In addition, a proxy contest for the election of directors at our annual meeting would require us to incur significant legal fees and

proxy solicitation expenses and require significant time and attention by management and our board of directors. The perceived uncertainties as to our future direction also could affect the market price and volatility of our securities.

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

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

- the classification of our board of directors into three classes, with one class elected each year;
- prohibiting cumulative voting in the election of directors;
- the ability of our board of directors to issue preferred stock without stockholder approval;
- the ability to remove a director only for cause and only with the vote of the holders of at least 66 2/3% of our voting stock;
- a special meeting of stockholders may only be called by our chairman or Chief Executive Officer, or upon a resolution adopted by an affirmative vote of a majority of the board of directors, and not by our stockholders;
- prohibiting stockholder action by written consent; and
- our stockholders must comply with advance notice procedures in order to nominate candidates for election to our board of directors or to place stockholder proposals on the agenda for consideration at any meeting of our stockholders.

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

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

The following table provides information regarding our purchases of shares of our common stock during the thirteen weeks ended July 31, 2016 related to our stock repurchase program:

Period ⁽¹⁾	Total Number of Shares Purchased ⁽²⁾	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs ⁽²⁾	Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs ⁽²⁾
May 2, 2016 - May 29, 2016	200,913	\$ 63.65	200,913	\$ 48
May 30, 2016 - July 3, 2016	—	—	—	—
July 4, 2016 - July 31, 2016	—	—	—	—
Total	200,913		200,913	

⁽¹⁾ Monthly information is presented by reference to our fiscal periods during our second quarter of fiscal 2016 .

⁽²⁾ Our stock repurchase program was approved by our board of directors in June 2014. Common shares were repurchased in the open market at prevailing market prices, including under written plans complying with the provisions of Rule 10b5-1 and Rule 10b-18 of the Securities Exchange Act of 1934, with the timing and actual number of common shares repurchased depending upon market conditions, eligibility to trade, and other factors. The maximum dollar value of shares to be repurchased was \$450 million and the program was completed in the second quarter of fiscal 2016.

The following table provides information regarding our purchases of shares of our common stock during the thirteen weeks ended July 31, 2016 related to our Employee Share Purchase Plan:

Period ⁽¹⁾	Total Number of Shares Purchased ⁽²⁾	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs ⁽²⁾	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs ⁽²⁾
May 2, 2016 - May 29, 2016	9,894	\$ 63.53	9,894	5,126,044
May 30, 2016 - July 3, 2016	13,619	70.93	13,619	5,112,425
July 4, 2016 - July 31, 2016	8,129	77.73	8,129	5,104,296
Total	31,642		31,642	

⁽¹⁾ Monthly information is presented by reference to our fiscal periods during our second quarter of fiscal 2016 .

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

Excluded from this disclosure are shares repurchased to settle statutory employee tax withholding related to the vesting of stock-based compensation awards.

ITEM 6. EXHIBITS

Exhibit No.	Exhibit Title	Filed Herewith	Incorporated by Reference		
			Form	Exhibit No.	Filing Date
31.1	Certification of Chief Executive Officer Pursuant to Exchange Act Rule 13a-14(a)	X			
31.2	Certification of Chief Financial Officer Pursuant to Exchange Act Rule 13a-14(a)	X			
32.1*	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002				
101	The following unaudited interim consolidated financial statements from the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended May 1, 2016, formatted in XBRL: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Operations and Comprehensive Income, (iii) Consolidated Statements of Stockholders' Equity, (iv) Consolidated Statements of Cash Flows (v) Notes to the Unaudited Interim Consolidated Financial Statements	X			

* Furnished herewith

SIGNATURES

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

lululemon athletica inc.

By: /s/ S TUART H ASELDEN

Stuart Haselden

*Chief Financial Officer
(Principal Financial Officer and
Principal Accounting Officer)*

Dated: September 1, 2016

Exhibit Index

Exhibit No.	Exhibit Title	Filed Herewith	Incorporated by Reference		
			Form	Exhibit No.	File No.
31.1	Certification of Chief Executive Officer Pursuant to Exchange Act Rule 13a-14(a)	X			
31.2	Certification of Chief Financial Officer Pursuant to Exchange Act Rule 13a-14(a)	X			
32.1*	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002				
101	The following unaudited interim consolidated financial statements from the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended May 1, 2016, formatted in XBRL: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Operations and Comprehensive Income, (iii) Consolidated Statements of Stockholders' Equity, (iv) Consolidated Statements of Cash Flows (v) Notes to the Unaudited Interim Consolidated Financial Statements	X			

* Furnished herewith

I, Laurent Potdevin, certify that:

1. I have reviewed this quarterly report on Form 10-Q of lululemon athletica inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

By: /s/ L AURENT P OTDEVIN

Laurent Potdevin

Chief Executive Officer and Director

(Principal Executive Officer)

Date: September 1, 2016

I, Stuart Haselden, certify that:

1. I have reviewed this quarterly report on Form 10-Q of lululemon athletica inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

By: /s/ S TUART H ASELDEN

Stuart Haselden
Chief Financial Officer
(Principal Financial Officer and
Principal Accounting Officer)

Date: September 1, 2016

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906 OF
THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of lululemon athletica inc. (the "Company") on Form 10-Q for the second quarter of fiscal 2016 , as filed with the Securities and Exchange Commission on the date hereof (the "Report"), each of the undersigned officers of the Company certifies, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that, to such officer's knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

By: /s/ L AURENT P OTDEVIN
Laurent Potdevin
Chief Executive Officer and Director
(Principal Executive Officer)

Date: September 1, 2016

By: /s/ S TUART H ASELDEN
Stuart Haselden
Chief Financial Officer
(Principal Financial Officer)

Date: September 1, 2016

The foregoing certification is being furnished solely pursuant to 18 U.S.C. § 1350 and is not being filed as part of the Report or as a separate disclosure document.