

DECKERS OUTDOOR CORP  
Form DFAN14A  
October 05, 2017

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

**SCHEDULE 14A**

**(Rule 14a-101)**

**SCHEDULE 14A INFORMATION**

**Proxy Statement Pursuant to Section 14(a) of the**  
**Securities Exchange Act of 1934**

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

Preliminary Proxy Statement

**Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**

Definitive Proxy Statement

Definitive Additional Materials

Soliciting material Pursuant to §240.14a-12

**Deckers Outdoor Corporation**

**(Name of Registrant as Specified In Its Charter)**

**MARCATO INTERNATIONAL MASTER FUND, LTD.**

**MARCATO CAPITAL MANAGEMENT LP**

**MCM ENCORE IM LLC**

**MARCATO ENCORE MASTER FUND, LTD.**

**RICHARD T. MCGUIRE III**

**DEBORAH M. DERBY**

**KIRSTEN J. FELDMAN**

**STEVE FULLER**

**MATTHEW P. HEPLER**

**ROBERT D. HUTH**

**JAN ROGERS KNIFFEN**

**MITCHELL A. KOSH**

**NATHANIEL J. LIPMAN**

**MICHAEL W. RAYDEN**

**ANNE WATERMAN**

**(Name of Person(s) Filing Proxy Statement, if other than the Registrant)**

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4) Date Filed:

On October 4, 2017, Marcato Capital Management LP and certain affiliates issued the following presentation at the Sohn San Francisco Investment Conference regarding Deckers Outdoor Corporation:

Sohn Conference October 2017

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Overview: Deckers (“DECK”) Ticker: “DECK” Recent Stock Price: \$66 Source: Company filings, CapitalIQ. Market data as of 9/26/17 Multi-branded footwear and apparel company: UGG Hoka One One Sanuk Teva Consensus Estimates (FYE 3/31/18E): 2018E EBITDA: \$239 million 2018E EPS: \$4.08 Valuation (FYE 3/31/18E): EV/EBITDA: 8x P/E: 16x Capitalization: Market Cap: \$2.1 billion Enterprise Value: \$1.9 billion Current Investment: 2nd largest position in fund Average Cost: \$46 Beneficial Ownership: 6.1%



Deckers brand overview Item UGG Product Type Comfort Shoes & Apparel Running Shoes Casual Shoes Outdoor Shoes & Sandals Revenue FYE 3/31/17 \$1,451m ~\$115m \$92m \$118m Growth Profile Mature grower Rapid growth Low growth Low growth (1) Source: Company filings, Marcato estimates See appendix for footnotes

Why we invested in deckers UGG is a substantial footwear brand that generates strong cash flows, returns and is underpenetrated internationally Hoka One One is a rapidly growing running shoe brand whose value is not recognized by the market Significant share price and operational underperformance due to failed brick & mortar expansion and unchecked expense growth Marcato sees opportunities to enhance shareholder value: Focus on core UGG brand, pursue sale or spin-off of non-core brands Hire strategy consultants to implement efficiency program targeting aggressive retail closures, corporate cost reduction and supply chain efficiencies Recapitalize balance sheet with initial target leverage ratio of 1x Net Debt/EBITDA Use proceeds of recapitalization and sale of brands to repurchase shares Align management compensation with margin, return and TSR improvement See appendix for footnotes

ugg is a large & established brand in casual footwear UGG Brand Revenue (\$M)(1) Note: 2005-2013 are 12/31 fiscal end. 2014-2017 are 3/31 fiscal end. Due to a change in reporting period, the company has no 2014 fiscal year. 2014 above is the LTM period through 3/31/14 Source: Company filings, Wall Street Research See appendix for footnotes Estimated sales of casual footwear brands (\$M)(2) 19% CAGR

Retail expansion has damaged ROIC and EBIT margins Note: 2006-2013 are 12/31 fiscal end. 2014-2017 are 3/31 fiscal end. Due to a change in reporting period, the company has no 2014 fiscal year. 2014 above is the LTM period through 3/31/14 Source: Company filings See appendix for footnotes Company ROIC using gross debt+Equity(1)  
(3)(4) Which ROIC definition do we want to use? I switched this to net debt + equity (instead of gross debt + equity).  
Terex uses net debt. (1) (2) (2) (3) Significant retail expansion

SG&A and Unallocated Overhead have grown faster than revenue SG&A Unallocated Overhead % of Revenue Note: 2011-2013 are 12/31 fiscal end. 2014-2017 are 3/31 fiscal end. Due to a change in reporting period, the company has no 2014 fiscal year. 2014 above is the LTM period through 3/31/14 Source: Company filings See appendix for footnotes (1) Unallocated overhead

I. Focus on Core UGG Brand, Exit Non-Core Brands

Poor history of investing capital into non-ugg brands Last year Deckers wrote-down the asset value of its Sanuk brand by over 60% Sanuk writedown Other Brands Wholesale segment (\$M) Note: 2011-2013 are 12/31 fiscal end. 2014-2017 are 3/31 fiscal end. Due to a change in reporting period, the company has no 2014 fiscal year. 2014 above is the LTM period through 3/31/14 Source: Company filings, CapIQ Target Type of Footwear Price Paid Hoka One One Running Shoe Unknown Sanuk Sandal \$149.8 Ahnu Active footwear/hiking \$10.5 TSUBO Casual, but Deckers exited in 2016 \$5.9 Acquired brands

Opportunity to Unlock Value From Non-Core Brands Source: Marcato estimates



## II. Rationalize Retail Footprint

Retail Expansion Continued Despite Declining Metrics Retail stores (Year end) Retail EBIT and Margins (2)(3) Note: 2011-2013 are 12/31 fiscal end. 2014-2017 are 3/31 fiscal end. Due to a change in reporting period, the company has no 2014 fiscal year. 2014 above is the LTM period through 3/31/14 Source: Company filings, Marcato estimates See appendix for footnotes Δ in Retail Same Store Sales (1) (1) 3.4% 2.8% NA (8.4%) 6.3% NA NA Without adj. for Restructuring & Impairment: ~\$6m EBIT, 2% margin (3) (3) \$3.2 \$2.9 \$2.9 \$2.7 \$4.2 Est. \$2.5 Est. \$2.3 Revenue per Store(\$m) (4) (5) (5)

Ecommerce and Retail Segments Were Combined To Hide Retail Weakness Direct to Consumer EBIT Breakdown  
Direct to Consumer EBIT % Margin Note: 2011-2013 are 12/31 fiscal end. 2014-2017 are 3/31 fiscal end. Due to a  
change in reporting period, the company has no 2014 fiscal year. 2014 above is the LTM period through 3/31/14  
Source: Company filings, Marcato estimates See appendix for footnotes In 2016, Deckers combined its E-Commerce  
and Retail segments into a single segment called Direct to Consumer (DTC). This combination in reporting makes it  
very difficult to isolate retail results. A modest decline in E-Commerce margins would imply a single digit margin for  
retail in FY2016 and FY2017 \$102 Reported Ex. Rest. & Impair. (4) (1) (2) (2) (5) \$110 Reported Ex. Rest. & Impair.  
(5) (5)(6) (3) (3)

Retail profitability significantly lower after allocating overhead Retail EBIT % Margin Before and After Estimated Corporate Allocation Retail ROA Before and After estimated corporate allocation(4)(5) Note: 2011-2013 are 12/31 fiscal end. 2014-2017 are 3/31 fiscal end. Due to a change in reporting period, the company has no 2014 fiscal year. 2014 above is the LTM period through 3/31/14 Source: Company filings, Marcato estimates See appendix for footnotes (2)(3) (4) (2)(3) (4) (1) (1) (1) (1) (2)(3)

Retail Stores would benefit from Margin Improvement Or Closure After allocating corporate expenses, average profitability levels need to more than double to improve retail segment margins above Deckers' cost of capital Source: Company filings, Marcato estimates See appendix for footnotes Est. DECK 2016 Above cost of capital

### III. Optimize Profitability

“...we are pleased to share that \$150 million announced cumulative savings will drive a \$100 million improvement in operating profit for the fiscal year 2020 [relative to 2017]. With these savings, along with modest low single-digit revenue growth, we believe we can achieve an operating margin of 13% in fiscal year 2020.” – 5/25/17 FQ4 2017 earnings call Deckers Has Announced Profit Improvement Goals xx Source: Company filings, Marcato estimates Misleading statements \$100m of “operating income improvement” is not equivalent to “net bottom line savings” This is because some of the \$100m operating income will be generated by future revenue growth After accounting for incremental operating income generated by growth, we estimate that savings targets are only ~\$50-60m Many analysts and investors have interpreted this operating income improvement as “net saving” \$63m of EBIT would be generated alone from future revenue growth at a 30% incremental margin Using Deckers’ 2020 guidance of \$2b in sales and a 13% EBIT margin, implied EBIT improvement is \$94m -- slightly below Deckers’ target of \$100m Deckers announcement of savings program This implies only ~\$30m in EBIT improvement from cost savings

Efficiency Consultants Estimate Savings Opportunity of \$150-\$200M Best in class consultant that has worked with leading footwear and apparel companies including Nike, Adidas, Timberland and Wolverine Worldwide has identified \$150-\$200m of savings potential xx Source: External consulting firm estimates Item Description Opportunity Rationalize Retail Optimize network Improve store operations Revise trade terms and inventory \$40-\$50m Reduce SG&A Bring in-line with peer benchmarks Personnel reductions Selective outsourcing Optimize indirect costs \$50-70m Reduce COGS Optimize assortment Supplier negotiations \$50-70m Other Opportunities \$10m Total \$150-200m



#### IV. Wolverine Case Study

Wolverine cost savings Program Retail Footprint Rationalization In process of reducing total stores from 466 stores in 2013 to ~80 going forward Exited all Stride Rite stores and converted wholesale business to a licensing model to improve ROIC Post rationalization, Stride Rite generates similar EBIT at higher margins, requires less working capital, fewer resources, and reduces markdown risk 2017 revenue expected to be reduced by \$125m-\$175m with operating profitability improving \$20m Portfolio Rationalization Divested or discontinued smaller brands Robeez, Sebago, and Cushe Streamlined global supply chain Consolidated factory base by nearly 1/3 by end of 2016 130-200bps estimated benefit to margin Disciplined capital structure and allocation Announced \$300m share repurchase program Refinanced debt to ~1.8x net debt to EBITDA(1) Improved FCF and WC turns with asset light model Significant FCF improvement and working capital release with retail footprint rationalization Wolverine Worldwide provides a comparable case study WWW One-year Share price performance Source: Company Filings, Wall street research See appendix for footnotes

V. Valuation Impact

Before revenue growth, marcato's optimization plan would drive earnings Non-UGG brands monetized Conservative revenue assumptions for remaining UGG based on public target EBIT increases over 75% Margins double Retail EBIT improves with rationalization Unallocated corporate declines with cost program EPS increases over 230% Over 50% of shares repurchased ROIC increases over 80% Note: Company's fiscal year ends 3/31 Source: Company filings, Marcato estimates. Market data as of 9/26/17 (1)

Marcato proposal(1) Marcato Believes Deckers' stock price Has over 2x opportunity over 3 year horizon Potential value creation for deckers| FY2017A – FY2020E Note: Company's fiscal year ends 3/31 Source: Company filings, Marcato estimates. Market data as of 9/26/17 20% 26% 31% ROIC(1) EPS 7.0x 7.5x EV/EBITDA 24 17 15 Ending Shares Outstanding FY2018E FY2019E FY2020E Marcato Proposal (Margin improvement, divestitures and share repurchases) \$158@ 8.0x EBITDA \$146@ 7.5x EBITDA \$135@ 7.0x EBITDA Recent Price: \$66 11% 16% 19% EBIT % Margin \$4.23 \$7.29 \$11.64 +82% (53%) +108% FY2017 17% 32 9% Δ 2017 – 2021E +232% 32% 15 FY2021E 19% \$12.68 \$3.82 Currently assuming an average share price of \$70 for the initial levered recap, after that shares appreciate 15% a year. (2) (2) (3%) 2.6% 3.2% Core UGG Revenue Growth 2.0% 1.2% CAGR (3)

Appendix: Footnotes Page 4 Marcato estimate Page 6 Includes UGG brand revenue from both the wholesale and direct to consumer channels Sourced from company filings and a Buckingham 3/3/2017 research report Page 7 ROIC Defined as  $(EBIT \times (1 - \text{Tax Rate})) / (\text{Average period net PPE} + \text{Working capital})$ . Working capital defined as  $(\text{Current assets} - \text{cash}) - (\text{Current liabilities} - \text{short term debt})$  2016 based on adjusted EBIT (ex. restructuring) of \$196m; 2017 based on adjusted EBIT (ex. restructuring) of \$166m Assumes normalized tax rate of 27% (similar to 2018 guidance) Page 8 2017 SG&A excludes \$167.5m in restructuring and other charges Page 13 Retail EBIT reporting methodology was changed in 2013. The 2012 and 2011 EBIT numbers are pro forma for the reporting change Beginning in 2016 company combined its legacy retail segment with E-Commerce to form the Direct-to-Consumer (DTC) segment. Total 2016 DTC segment revenue was \$644m and EBIT was \$102m. Estimate that E-Commerce revenue was \$265m with a ~36% EBIT margin (2015 E-Commerce margin was ~40% but believe margins came down somewhat due to promotional pricing), implying an E-Commerce EBIT estimate of ~\$95m. The implied retail portion of the DTC segment is therefore ~\$379m of revenue and \$6m of EBIT, which would give an implied retail margin of ~2% (this is unadjusted for unusual items, see footnote 3) Adjusted for unusual items. Adjusted to exclude \$11m of retail fleet restructuring expense and \$10m of other retail related impairment charges (which would imply an adjusted retail EBIT margin of 7% vs the estimated 2% unadjusted retail EBIT margin) Estimate that the e-commerce business did \$295m in revenue in FY2017 at a ~35% margin, which would imply \$103m of e-commerce EBIT and \$7m of retail EBIT (given that total DTC EBIT was \$110m) Adjusted for unusual items. Adjusts for \$12.9m in DTC restructuring costs (assume these are all retail related) Page 14 Adjusted to exclude \$11m of retail fleet restructuring expense and \$10m of other retail related impairment charges Retail EBIT reporting methodology was changed in 2013. The 2012 and 2011 EBIT numbers are pro forma for the reporting change Adjusted for unusual items. Margins adjusted for restructuring and impairment charges related to the retail segment. Reported DTC margin was 16%, but adjusted for \$11m of restructuring and \$10m of impairment would be 19%. Estimate retail without adjusting for unusual items was 2%, but after adjusting for restructuring and impairment was 7%. See footnote 4 Total reported 2016 DTC segment revenue was \$644m and EBIT was \$102m. Estimate that E-Commerce revenue was \$265m with a ~36% EBIT margin (2015 E-Commerce margin was ~40% but believe margins came down somewhat due to promotional pricing), implying an E-Commerce EBIT estimate of ~\$95m. The implied retail portion of the DTC segment is therefore ~\$379m of revenue and \$6m of EBIT, giving an implied retail margin of ~2%. Further adjusting retail to exclude \$11m of retail fleet restructuring expense and \$10m of impairment charges would increase the retail EBIT margin to ~7% (and increase the combined DTC margin to ~19%) Adjusted for unusual items. Excludes \$13m in restructuring charges (assume related to retail transformation) Assumes an E-Commerce margin of 35% and that all restructuring charges are retail related Page 15 Retail EBIT reporting methodology was changed in 2013. The 2012 and 2011 EBIT numbers are pro forma for the reporting change Adjusted to exclude restructuring expenses of \$11m and impairment charges of \$10m in 2016. Adjusted to exclude \$13m of restructuring in 2017 2016 and 2017 are a best estimate because company stopped reporting the segment Allocates a portion of unallocated corporate overhead to the retail segment based on retail revenue as a percentage of total company revenue ROA defined as  $(\text{Retail EBIT} \times (1 - \text{Tax Rate})) / (\text{Average quarterly retail assets during the period})$  Page 16 FY2015 is the last year the company disclosed retail segment financials. In 2015 unallocated overhead was \$221m and the retail segment made up 21% of revenue. If the corporate overhead is allocated to individual segments based on revenue, then the retail allocation of corporate overhead would have been \$47m. The company had 142 stores at the time, which would imply that the corporate overhead per retail store was \$0.33m (~\$47m of corporate overhead allocated to retail, divided by 142 stores) Page 21 Net debt/LTM EBITDA as of Q4 2016 (period when the debt refinancing was finalized) Page 23 EPS ex. restructuring items Page 24 ROIC Defined as  $(EBIT \times (1 - \text{Tax Rate})) / (\text{Average period net PPE} + \text{Working capital})$  Based on adjusted EBIT (ex. restructuring) of \$166m and an assumed normalized tax rate of 27% EPS ex. restructuring items