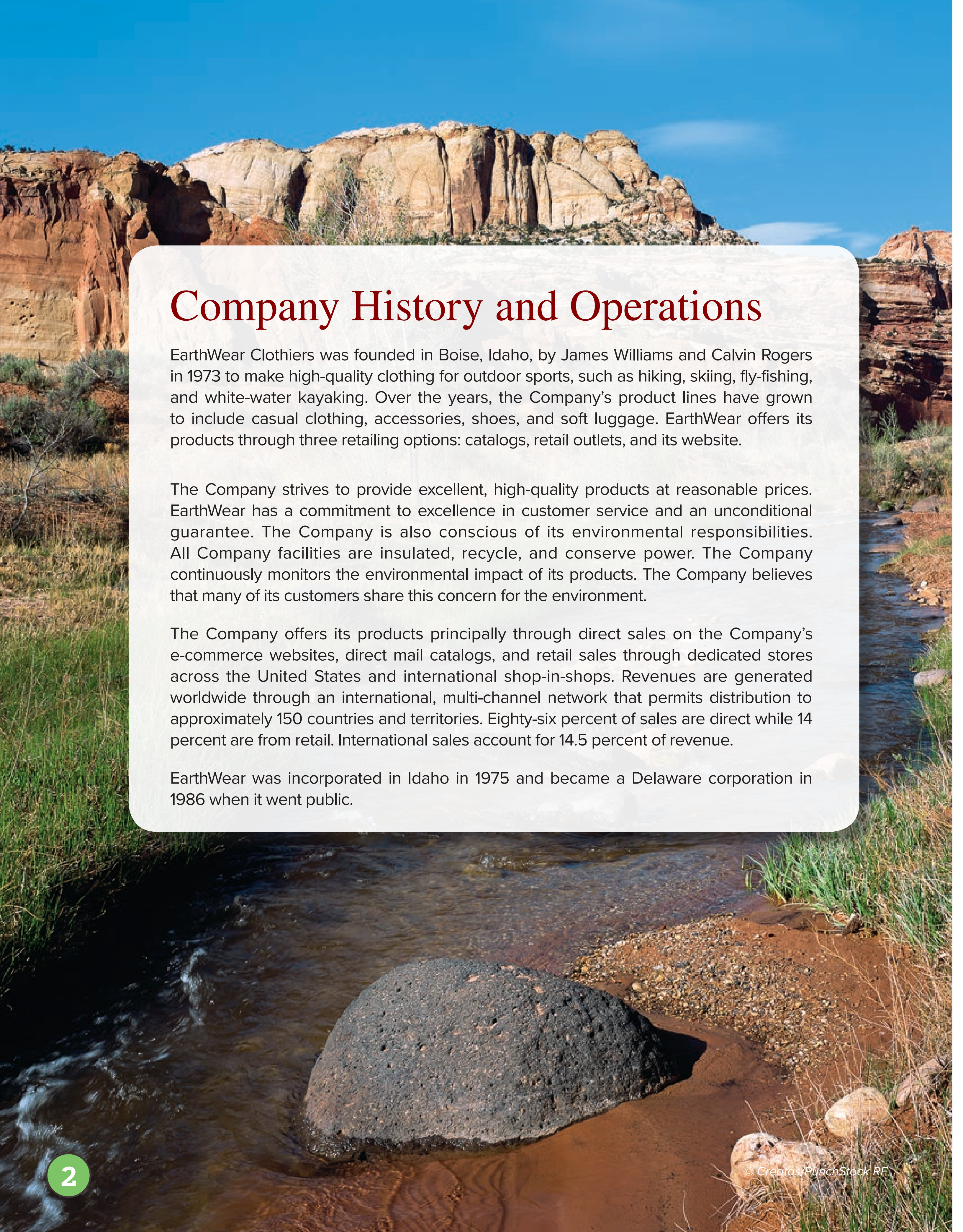
ANNUAL REPORT

EarthWear

2018



Company History and Operations

EarthWear Clothiers was founded in Boise, Idaho, by James Williams and Calvin Rogers in 1973 to make high-quality clothing for outdoor sports, such as hiking, skiing, fly-fishing, and white-water kayaking. Over the years, the Company's product lines have grown to include casual clothing, accessories, shoes, and soft luggage. EarthWear offers its products through three retailing options: catalogs, retail outlets, and its website.

The Company strives to provide excellent, high-quality products at reasonable prices. EarthWear has a commitment to excellence in customer service and an unconditional guarantee. The Company is also conscious of its environmental responsibilities. All Company facilities are insulated, recycle, and conserve power. The Company continuously monitors the environmental impact of its products. The Company believes that many of its customers share this concern for the environment.

The Company offers its products principally through direct sales on the Company's e-commerce websites, direct mail catalogs, and retail sales through dedicated stores across the United States and international shop-in-shops. Revenues are generated worldwide through an international, multi-channel network that permits distribution to approximately 150 countries and territories. Eighty-six percent of sales are direct while 14 percent are from retail. International sales account for 14.5 percent of revenue.

EarthWear was incorporated in Idaho in 1975 and became a Delaware corporation in 1986 when it went public.

COMPANY GROWTH STRATEGY EarthWear's growth strategy has three elements. First, the Company attempts to increase sales by expanding its customer base and by increasing sales to existing customers through improved product offerings. Second, the Company seeks to generate additional sales by targeted emails and mailings of special issues of its catalogs. Third, the Company is pursuing additional opportunities to expand its merchandising skills internationally.

E-COMMERCE The Company is a leading digital brand in the apparel industry. One of our goals is to broaden our customer base by creating engaging shopping experiences through our e-commerce platforms. To this end, we launched a significantly improved and redesigned new website which includes:

- Streamlined checkout to capture an increasing share of sales as customers migrate to mobile devices.
- Convenient payment types especially from mobile devices.
- Improved search, navigation, and our recommendation engine that provide great solutions for customers to quickly find products that best fulfill their product and style preferences.
- Enhanced digital E-catalogs, which allow prospective and existing customers to view, engage, and shop our products in innovative ways.

CATALOG OPERATIONS During 2018 the Company mailed 12 issues of its regular monthly catalog with an average of 75 pages per issue from its U.S. operations. Worldwide, the Company mailed approximately 160 million full-price catalogs. EarthWear views each catalog issue as a unique opportunity to communicate with its customers. Products are described in visual and editorial detail, and the Company uses such techniques as background stories and distinctive covers to stimulate the readers' interest.

Each issue of the regular catalog offers certain basic product lines for men and women. The regular catalog also offers seasonal merchandise. In addition, EarthWear mails two end-of-season clearance catalogs. The Company mails its catalogs to prospective customers who are identified based on lists of magazine subscribers and lists of households meeting certain demographic criteria. In addition, the Company identifies prospective new customers through its national advertising campaign.

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CUSTOMER DATABASE A principal factor in the Company's success has been the development of our list of existing and prospective households, many of whom were identified by their responses to our marketing. The Company routinely updates and refines our customer list prior to individual catalog and email mailings and monitors customer interest in our offerings as reflected by criteria such as the timing and frequency of purchases and the dollar amount of and types of products purchased. The customer base consists primarily of affluent, college-educated, professional, and style-conscious women and men. In 2018, customers had average annual household income of $104,000 and the average age of our customer is 45, according to an analysis of our customer file using demographic, behavioral, lifestyle, financial, and home attribute databases.

PRODUCT DEVELOPMENT EarthWear concentrates on clothing and other products that are aimed at customers interested in outdoor activities. The Company's products are styled and quality crafted to meet the changing tastes of the Company's customers rather than to mimic the changing fads of the fashion world. At the same time, the Company seeks to maintain customer interest by developing new products, improving existing core products, and reinforcing its value positioning.

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The Company continues to incorporate innovations in fabric, construction, and detail that add value and excitement and differentiate EarthWear from the competition. In order to ensure that products are manufactured to the Company's quality standards at reasonable prices, product managers, designers, and quality assurance specialists develop the Company's own products.

EarthWear deals directly with its suppliers and seeks to avoid intermediaries. All goods are produced by independent manufacturers except for most of its soft luggage, which is assembled at the Company's facilities. During 2018, the Company purchased merchandise from approximately 300 domestic and foreign manufacturers. One manufacturer and one intermediary accounted for about 14 and 29 percent of the Company's received merchandise, respectively, in 2018. In 2018, about 80 percent of the Company's merchandise was imported, mainly from Asia, Central America, Mexico, and Central America. The Company will continue to take advantage of worldwide sourcing without sacrificing customer service or quality standards.

Order Entry, Fulfillment, and Delivery

The majority of EarthWear sales are made through its e-commerce platforms. The Company also has toll-free telephone numbers that customers can call 24 hours a day, seven days a week (except Christmas Day) to place orders or to request a catalog. Telephone calls are answered by the Company's well-trained sales representatives, who enter customer orders and retrieve information about product characteristics and availability.

The Company's order entry and fulfillment system permits shipment of in-stock orders on the following day, but orders requiring monogramming or inseaming typically require one or two extra days. The Company's sales representatives enter orders into an online order entry and inventory control system. Customers using the Company's Internet site see color photos of the products, their availability, and prices. When ordering a product over the Internet, the customer completes a computer screen that requests information on product code, size, color, and so on. When the customer finishes shopping for products, he or she enters delivery and credit card information. EarthWear provides assurance through CPA *WebTrust* SM that the website has been evaluated and tested to meet *WebTrust* SM principles and criteria. This assurance service is provided by the Company's independent auditors, Willis & Adams, LLP.

Orders are generally shipped by United Parcel Service (UPS) at various tiered rates that depend on the total dollar value of each customer's order. Other expedited delivery services are available at additional charge. Domestically, the Company utilizes two-day UPS service at standard rates, enhancing its customer service. Comparable services are offered in international markets.

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MERCHANDISE LIQUIDATION Liquidations (sales of overstock and end-of-season merchandise at reduced prices) were approximately 12 percent, 11 percent, and 8 percent of net sales in 2018, 2017, and 2016, respectively. The balance was sold principally through the Company's outlet retail stores.

COMPETITION The Company's principal competitors are retail stores, including specialty shops, department stores, and other catalog companies. Direct competitors include Eddie Bauer, Land's End, L. L. Bean, Patagonia, and Timberland. The Company may also face increased competition from other retailers as the variety of merchandise offered over the Internet increases. The apparel retail business in general is intensely competitive. EarthWear competes principally on the basis of merchandise value (quality and price), its established customer list, and customer service, including fast order fulfillment and its unqualified guarantee.

TRADEMARKS The Company uses the trademarks of "EarthWear" and "EWC" on products and catalogs.

SEASONALITY OF BUSINESS The Company's business is highly seasonal. Historically, a disproportionate amount of the Company's net sales and most of its profits have been realized during the fourth quarter. If the Company's sales were materially different from seasonal norms during the fourth quarter, the Company's annual operating results could be materially affected. Accordingly, results for the individual quarters do not necessarily indicate results to be expected for the entire year. In 2018, 37 percent of the Company's total revenue came in the fourth quarter.

EMPLOYEES The Company believes that its skilled and dedicated workforce is one of its key resources. Employees are not covered by collective bargaining agreements, and the Company considers its employee relations to be excellent. As a result of the highly seasonal nature of the Company's business, the size of the Company's workforce varies, ranging from approximately 3,500 to 5,300 individuals in 2018. During the peak winter season of 2018, approximately 2,700 of the Company's 5,300 employees were temporary employees.

EXECUTIVE OFFICERS OF THE COMPANY

James G. Williams, is chairman of the board and former chief executive officer. Mr. Williams was one of the two original founders of EarthWear. He stepped down as chief executive officer in December 1999.

Calvin J. Rogers, is president and chief executive officer of the Company. Mr. Rogers was one of the two original founders of the Company. He assumed his present position in December 1999.

Dominique DeSantiago, is executive vice president and chief operating officer. Mr. DeSantiago joined the Company as chief operating officer in June 1991. He was promoted to vice president in October 1994. Mr. DeSantiago was previously employed by Eddie Bauer in various capacities.

Linda S. McDaniel, is senior vice president of sales. She joined the Company in July 1996. Ms. McDaniel served as divisional vice president, merchandising, with Patagonia between 1986 and 1990. Ms. McDaniel was the president and chief executive officer for Mountain Goat Sports from 1990 until 1996. She has been serving as a director of the Company since November 1997.

James C. ("JC") Watts, is senior vice president and chief financial officer. Mr. Watts joined the Company in May 1996, assuming his current position. He was previously employed by Federated Department Stores.

Mary Ellen Tornesello, is senior vice president of operations. Ms. Tornesello joined the Company in 1994 as operations manager. She served as vice president of operations from 1995 until 1997, at which time she assumed her present position.

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Market information The common stock of the Company is listed and traded on NASDAQ under the symbol EWCC. The high and low prices of the Company's common stock for 2018 were $52.50 and $21.75 per share. The closing price of the Company's stock on December 31, 2018, was $26.75 per share.

Shareholders As of December 31, 2018, the number of shareholders of record of common stock of the Company was 2,120. This number excludes shareholders whose stock is held in nominee or street name by brokers.

Independent Auditors The Company has been audited by Willis & Adams since incorporation in 1975.

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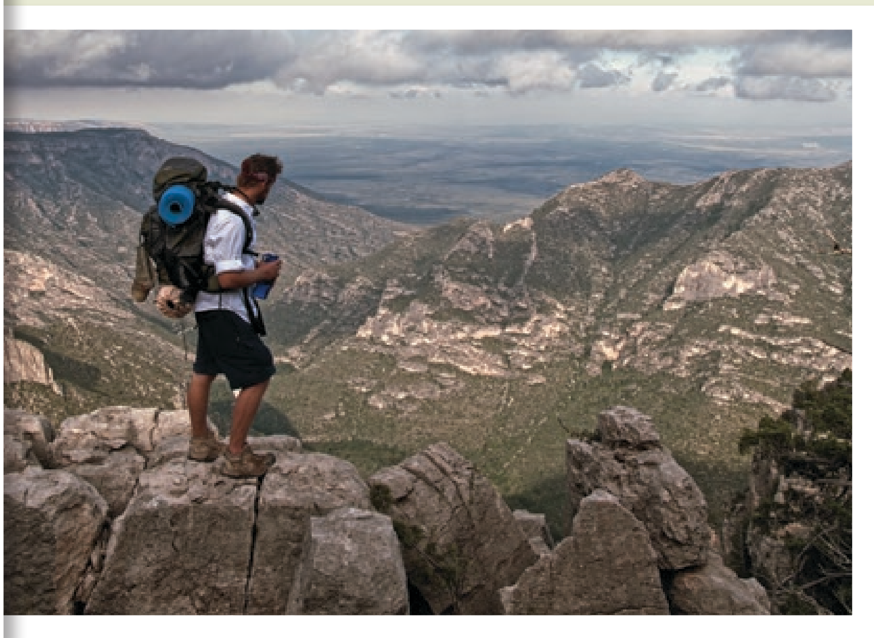
EARTHWEAR CLOTHIERS

Consolidated Statements of Comprehensive Income

(In thousands, except share data)

	For the period ended December 31		
	2018	2017	2016
Net Sales	**$ 950,484**	$ 857,885	$ 891,394
Cost of sales	**546,393**	472,739	490,530
Gross Profit	**404,091**	385,146	400,864
Selling, general, and administrative expenses	**364,012**	334,994	353,890
Nonrecurring charge (credit)	—	(1,153)	8,190
Income from operations	**40,079**	51,305	38,784
Other income (expense):			
Interest expense	**(983)**	(1,229)	(5,027)
Interest income	**1,459**	573	10
Other	**(4,798)**	(1,091)	(1,593)
Total other income (expense), net	**(4,322)**	(1,747)	6,610
Income before income taxes	**35,757**	49,558	32,174
Income tax provision	**13,230**	18,337	11,905
Net income	**$ 22,527**	$ 31,221	$ 20,269
Other Comprehensive Income:			
Foreign currency translation adjustments	**(1,151)**	437	733
Unrealized gain on forward contracts	**3,295**		
Other comprehensive income (loss), net of tax	**2,144**	437	733
Comprehensive Income	**$ 24,671**	$ 31,658	$ 21,002
Net Income per Common Share:			
Basic earnings per share	**1.15**	1.60	1.02
Diluted earnings per share	**1.14**	1.56	1.01
Basic weighted average shares outstanding	**19,531**	19,555	19,806
Diluted weighted average shares outstanding	**19,774**	20,055	19,996



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EARTHWEAR CLOTHIERS

Consolidated Balance Sheets

(In thousands)

Assets	December 31 2018	2017
Current assets:		
Cash and cash equivalents	**$ 48,978**	$ 49,668
Receivables, net	**12,875**	11,539
Inventory	**122,337**	105,425
Prepaid advertising	**11,458**	10,772
Other prepaid expenses	**6,315**	3,781
Deferred income tax benefits	**7,132**	6,930
Total current assets	**209,095**	188,115
Property, plant, and equipment, at cost:		
Land and buildings	**70,918**	66,804
Fixtures and equipment	**62,003**	61,800
Computer hardware and software	**64,986**	47,466
Right-to-Own Leased Space and Equipment	**6,510**	6,076
Leasehold improvements	**2,010**	1,894
Total property, plant, and equipment	**206,427**	184,040
Less accumulated depreciation and amortization	**85,986**	76,256
Property, plant, and equipment, net	**120,441**	107,784
Intangibles, net	**423**	628
Total assets	**$ 329,959**	$ 296,527

Liabilities and Stockholders' Equity	2018	2017
Current liabilities:		
Lines of credit	**$ 11,011**	$ 7,621
Accounts payable	**59,009**	45,430
Reserve for returns	**5,890**	5,115
Accrued liabilities	**23,728**	25,364
Accrued profit sharing	**1,532**	1,794
Income taxes payable	**8,588**	6,666
Total current liabilities	**109,758**	91,990
Operating Lease Liability	**6,510**	6,076
Deferred income taxes	**9,469**	5,926
Stockholders' Equity:		
Common stock, 26,121 shares issued	**261**	261
Donated capital	**5,460**	5,460
Additional paid-in capital	**20,740**	19,311
Deferred compensation	**(79)**	(154)
Accumulated other comprehensive income	**3,883**	1,739
Retained earnings	**317,907**	295,380
Treasury stock, 6,546 and 6,706 shares at cost	**(143,950)**	(129,462)
Total Stockholders' Equity	**204,222**	192,535
Total liabilities and Stockholders' Equity	**$ 329,959**	$ 296,527

EARTHWEAR CLOTHIERS

Consolidated Statements of Cash Flows

(In thousands)

	For the period ended December 31		
Cash flows from (used for) operating activities:	**2018**	2017	2016
Net income	**$ 22,527**	$ 31,221	$ 20,270
Adjustments to reconcile net income to net cash flows from operating activities:			
Nonrecurring charge (credit)		(1,150)	8,190
Depreciation and amortization	**15,231**	13,465	12,175
Deferred compensation expense	**75**	103	424
Deferred income taxes	**3,340**	5,376	(3,866)
Loss on disposal of fixed assets	**284**	602	381
Changes in assets and liabilities excluding the effects of divestitures:			
Receivables, net	**(1,336)**	2,165	(3,666)
Inventory	**(16,912)**	37,370	13,954
Prepaid advertising	**(686)**	3,110	(1,849)
Other prepaid expenses	**(2,534)**	1,152	(1,628)
Accounts payable	**14,078**	(8,718)	2,716
Reserve for returns	**775**	439	692
Accrued liabilities	**(709)**	(4,982)	4,545
Accrued profit sharing	**(262)**	328	(1,320)
Income taxes payable	**1,923**	(2,810)	(3,834)
Tax benefit of stock options	**1,429**	1,765	349
Other	**2,144**	437	733
Net cash from (used for) operating activities	**39,367**	79,873	48,266
Cash flows from (used for) investing activities:			
Cash paid for capital additions	**(28,959)**	(18,208)	(30,388)
Net cash flows used for investing activities	**(28,959)**	(18,208)	(30,388)
Cash flows from (used for) financing activities:			
Proceeds from (payment of) short-term debt	**3,390**	(17,692)	4,228
Purchases of treasury stock	**(18,192)**	(2,935)	(23,112)
Issuance of treasury stock	**3,704**	4,317	1,199
Net cash flows used for financing activities	**(11,098)**	(16,310)	(17,685)
Net increase (decrease) in cash and cash equivalents	**(689)**	45,355	193
Beginning cash and cash equivalents	**49,668**	4,313	4,120
Ending cash and cash equivalents	**$ 48,978**	$ 49,668	$ 4,313
Supplemental cash flow disclosures:			
Interest paid	**$ 983**	$ 1,229	$ 5,027
Income taxes paid	**6,278**	13,701	18,107

EARTHWEAR CLOTHIERS

Consolidated Statements of Stockholders' Equity

(In thousands)

	Common Stock	Donated Capital	Additional Paid-In Capital	Deferred Compensation	Accumulated Other Comprehensive Income	Retained Earnings	Treasury Stock	Total
Balance, December 31, 2015	$261	$5,460	$17,197	$(681)	$569	$243,888	$(108,931)	$157,763
Purchase of treasury stock							(23,112)	(23,112)
Issuance of treasury stock							1,199	1,199
Tax benefit of stock options exercised			349					349
Deferred compensation expense				424				424
Net income						20,270		20,270
Other Comprehensive Income					733			733
Balance, December 31, 2016	$261	$5,460	$17,546	$(257)	$1,302	$264,158	($130,844)	$157,626
Purchase of treasury stock							(2,935)	(2,935)
Issuance of treasury stock							4,317	4,317
Tax benefit of stock options exercised			1,765					1,765
Deferred compensation expense				103				103
Net income						31,222		31,222
Other Comprehensive Income					437			437
Balance, December 31, 2017	$261	$5,460	$19,311	$(153)	$1,739	$295,380	$(129,462)	$192,535
Purchase of treasury stock							(18,192)	(18,192)
Issuance of treasury stock							3,704	3,704
Tax benefit of stock options exercised			1,429					1,429
Deferred compensation expense				75				75
Net income						22,527		22,527
Other Comprehensive Income					2,144			2,144
Balance, December 31, 2018	**$261**	**$5,460**	**$20,740**	**$(79)**	**$ 3,883**	**$317,907**	**$(143,950)**	**$204,222**

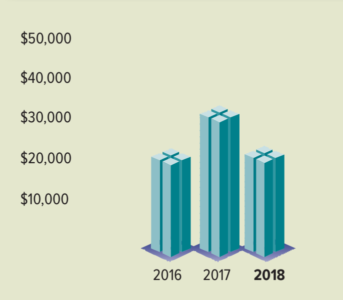
EARTHWEAR CLOTHIERS

Five-Year Consolidated Financial Summary (unaudited)

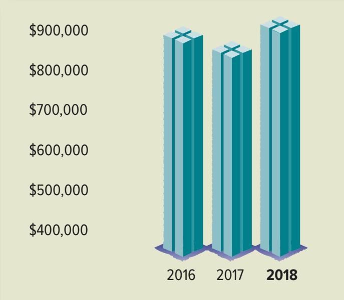
(In thousands, except per share data)

	For the period ended December 31				
	2018	2017	2016	2015	2014
Income statement data:					
Net Sales	**950,484**	857,885	891,394	821,359	503,434
Pretax Income	**35,757**	49,559	32,175	66,186	38,212
Percent of net sales	**3.8%**	5.8%	3.6%	8.1%	7.6%
Net income	**22,527**	31,222	20,270	41,698	22,929
Per share of common stock:					
Basic earnings per share	**1.15**	1.60	1.02	2.01	1.54
Diluted earnings per share	**1.14**	1.56	1.01	2.00	1.53
Common shares outstanding	**19,531**	19,555	19,806	20,703	14,599
Balance sheet data:					
Current assets	**209,095**	188,115	191,297	194,445	122,418
Current liabilities	**109,758**	91,990	133,434	118,308	65,505
PPE and intangibles	**120,864**	108,412	105,051	87,312	46,658
Total assets	**329,959**	296,527	296,347	281,757	170,121
Noncurrent liabilities	**15,979**	12,002	5,286	5,686	4,211
Shareholders' equity	**204,222**	192,535	157,627	157,763	100,405
Other data:					
Net working capital	**99,337**	96,125	57,863	76,137	56,913
Capital expenditures	**28,959**	18,208	30,388	31,348	8,316
Depreciation and amortization expense	**15,231**	13,465	12,175	9,833	6,101
Return on average shareholders' investment	**11%**	18%	13%	28%	24%
Return on average assets	**7%**	11%	7%	16%	15%

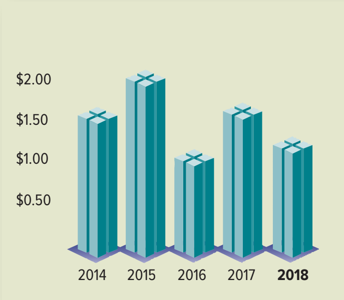
NET INCOME



NET SALES



NET INCOME PER SHARE



NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

NATURE OF BUSINESS EarthWear markets high quality clothing for outdoor sports, casual clothing, accessories, shoes, and soft luggage. The Company manages its business in three operating segments consisting of core, business-to-business, and international. The Company's primary market is the United States; other markets include Canada, Europe, and Japan.

PRINCIPLES OF CONSOLIDATION The consolidated statements include the accounts of the Company and its subsidiaries after elimination of intercompany accounts and transactions.

USE OF ESTIMATES The preparations of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results may differ from these estimates.

REVENUE RECOGNITION The Company records revenue at the time of shipment for catalog and e-commerce sales and at the point of sale for stores. The Company provides a reserve for returns.

RESERVE FOR LOSSES ON CUSTOMER RETURNS At the time of sale, the Company provides a reserve equal to the gross profit on projected merchandise returns, based on prior returns experience.

INVENTORY Inventory is stated at the last-in, first-out (LIFO) cost, which is lower than market. If the first-in, first-out method of accounting for inventory had been used, inventory would have been approximately $10.8 million and $13.7 million higher than reported at December 31, 2018 and 2017, respectively.

ADVERTISING The Company expenses the costs of advertising for magazines, television, radio, and other media the first time the advertising takes place, except for direct-response advertising, which is capitalized and amortized over its expected period of future benefits. Direct-response advertising consists primarily of catalog production and mailing costs, which are generally amortized within three months from the date catalogs are mailed.

DEPRECIATION Depreciation expense is calculated using the straight-line method over the estimated useful lives of the assets, which are 20 to 30 years for buildings and land improvements and 5 to 10 years for leasehold improvements and furniture, fixtures, equipment, and software. The Company allocates one half year of depreciation to the year of addition or retirement.

INTANGIBLES Intangible assets consist primarily of goodwill, and is not amortized but is tested at least annually for impairment.

FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK The Company uses import letters of credit to purchase foreign-sourced merchandise. The letters of credit are primarily U.S. dollar-denominated and are issued through third-party financial institutions to guarantee payment for such merchandise within the agreed-upon time periods. At December 31, 2018, the Company had outstanding letters of credit of approximately $23 million, all of which had expiration dates of less than one year.

FOREIGN CURRENCY TRANSLATIONS AND TRANSACTIONS Financial statements of the foreign subsidiaries are translated into U.S. dollars in accordance with ASC Topic 830. Translation adjustments are recorded in accumulated other comprehensive income, which is a component of stockholders' equity.

NOTE B: STOCKHOLDERS' EQUITY

COMMON STOCK The Company currently is authorized to issue 70 million shares of $0.01 par value common stock.

TREASURY STOCK The Company's board of directors has authorized the purchase of a total of 12.7 million shares of the Company's common stock. A total of 6.5 million and 6.7 million had been purchased as of December 31, 2018 and 2017, respectively.

STOCK AWARDS AND GRANTS The Company has a restricted stock award plan. Under the provisions of the plan, a committee of the Company's board may award shares of the Company's common stock to its officers and key employees. Such shares vest over a 10-year period on a straight-line basis.

The granting of these awards has been recorded as deferred compensation based on the fair market value of the shares at the date of the grant. Compensation expense under these plans is recorded as shares vest.

STOCK OPTIONS The Company has 3.5 million shares of common stock that may be issued pursuant to the exercise of options granted under the Company's stock option plan. Options are granted at the discretion of a committee of the Company's board of directors to officers and key employees of the Company. No option may have an exercise price less than the fair market value per share of the common stock at the date of the grant.

NOTE C: LINES OF CREDIT

The Company has unsecured domestic lines of credit with various U.S. banks totaling $150 million. In addition, the Company has unsecured lines of credit with foreign banks totaling the equivalent of $30 million for its wholly owned subsidiaries. At December 31, 2018, $11 million was outstanding at interest rates averaging 4.6 percent, compared with $7.6 million at December 31, 2017.

NOTE D: LONG-TERM DEBT

There was no long-term debt at December 31, 2018 and 2017.

NOTE E: LEASES

The Company leases store and office space and equipment under various lease arrangements. The leases are accounted for as operating leases. The Company has adopted ASC 842, *Leases*, which requires the recognition of lease in-use assets and lease liabilities on the balance sheet for leases with payments due over a year or more. In-use leased space and equipment for 2018 are $6,510 and for 2017 are $6,076.

NOTE F: RETIREMENT PLANS

The Company has a retirement plan that covers most regular employees and provides for annual contributions at the discretion of the board of directors. Included in the plan is a 401(k) feature that allows employees to make contributions.

MANAGEMENT'S DISCUSSION AND ANALYSIS:

2018 was a year during which we've seen the results of our strategic initiatives of the last two years take hold. Sales momentum picked up toward the end of the third quarter and continued strongly through our all-important holiday season, and we reported a double-digit increase in both revenue and earnings for the fourth quarter. This success enabled us to complete the year with an annual 10.8 percent increase in total revenue, but a 27.8 percent decrease in earnings, mainly due to the weakness of the first nine months. Our strong finish for the year was gratifying in the face of a difficult economy.

MANAGEMENT'S DISCUSSION AND ANALYSIS: RESULTS OF OPERATIONS FOR 2018 COMPARED TO 2017

TOTAL REVENUE INCREASED BY 10.8 PERCENT Total revenue for the year just ended was $950.5 million, compared with $857.9 million in the prior year, an increase of 10.8 percent. Seasonally strong sales resulted in a higher level of backorders during the fourth quarter and a first-time fulfillment rate of 85 percent for the year as a whole, slightly below the prior year's rate. Overall merchandise sales growth was primarily attributable to changes in circulation, which included adding back our post-Thanksgiving catalog and our January full-price catalog, shifting the timing of our fall/winter mailings, increasing page circulation and improving merchandise selection and creative presentations.

NET INCOME DECREASED Net income for 2018 was $22.5 million, down 27.8 percent from the $31.2 million earned in 2017. Diluted earnings per share for the year just ended were $1.14, compared with $1.56 per share for the prior year. The diluted weighted average number of common shares outstanding was 19.8 million for 2018 and 20.0 million for 2017.

GROSS PROFIT MARGIN Gross profit for the year just ended was $404 million, or 42.5 percent of total revenue, compared with $385 million, or 44.9 percent of total revenue, for the prior year. Liquidations were about 11 percent of net merchandise sales in 2018, compared with 12 percent in the prior year. In 2018, the cost of inventory purchases was down 2.0 percent, compared with deflation of 2.7 percent in 2017. This reduction was a result of improved sourcing. As a result, the LIFO inventory reserve was reduced by $2.8 million and $3.8 million in 2018 and 2017, respectively.

SELLING, GENERAL, AND ADMINISTRATIVE EXPENSES Selling, general, and administrative (SG&A) expenses increased 9.0 percent to $364 million in 2018, compared with $335 million in the prior year. As a percentage of sales, SG&A was 38.3 percent in 2018 and 39 percent in the prior year. The decrease in the SG&A ratio was primarily the result of lower catalog costs associated with increased page circulation, as well as lower information services expenses as we continued to invest in the Internet and upgrade systems capabilities. The cost of producing and mailing catalogs represented about 39 percent and 38 percent of total SG&A in 2018 and 2017, respectively.

CREDIT LINES AND CAPITAL EXPENDITURES Interest expense on lines of credit was down in 2018 due to lower average borrowing levels. Interest expense decreased to $1.0 million in 2018, compared to $1.2 million in 2017. We spent $29 million in cash on capital expenditures, which included $20 million for computer hardware and software. In addition, the Company acquired a new airplane by exchanging two of its own aircraft in 2018. Also, we purchased about $18 million in treasury stock. No long-term debt was outstanding at year-end 2018. Depreciation and amortization expense was $15.2 million, up 13.1 percent from the prior year, mainly due to computer software. Rental expense was $10.4 million, up 3.4 percent from 2017, primarily due to additional computer hardware.

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MANAGEMENT REPORT ON FINANCIAL STATEMENTS AND INTERNAL CONTROL OVER FINANCIAL REPORTING

To the Stockholders

EarthWear Clothiers, Inc.

Management of EarthWear Clothiers, Inc. (the "Company") is responsible for the preparation, consistency, integrity, and fair presentation of the consolidated financial statements. The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America applied on a consistent basis and, in management's opinion, are fairly presented. The financial statements include amounts that are based on management's informed judgments and best estimates.

Management has established and maintains comprehensive systems of internal control that provide reasonable assurance as to the consistency, integrity, and reliability of the preparation and presentation of financial statements; the safeguarding of assets; the effectiveness and efficiency of operations; and compliance with applicable laws and regulations. The concept of reasonable assurance is based upon the recognition that the cost of the controls should not exceed the benefit derived. Management monitors the systems of internal control and maintains an independent internal auditing program that assesses the effectiveness of internal control. Management assessed the Company's internal control over financial reporting for financial presentations in conformity with accounting principles generally accepted in the United States of America. This assessment was based on criteria for effective internal control over financial reporting established in *Internal Control—Integrated Framework* issued in 2013 by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO report). Based on this assessment, management believes that the Company maintained effective internal control over financial reporting for financial presentations in conformity with accounting principles generally accepted in the United States of America as of December 31, 2018.

The Board of Directors exercises its oversight role with respect to the Company's systems of internal control primarily through its Audit Committee, which is comprised solely of outside directors. The Committee oversees the Company's systems of internal control and financial reporting to assess whether their quality, integrity, and objectivity are sufficient to protect shareholders' investments.

The Company's consolidated financial statements have been audited by Willis & Adams LLP ("Willis & Adams"), independent auditors. As part of its audit, Willis & Adams considers the Company's internal control to plan the audit and determine the nature, timing, and extent of auditing procedures considered necessary to render its opinion as to the fair presentation, in all material respects, of the consolidated financial statements, which is based on independent audits made in accordance with the standards of the Public Company Accounting Oversight Board (United States). Management has made available to Willis & Adams all the Company's financial records and related data, and information concerning the Company's internal control over financial reporting, and believes that all representations made to Willis & Adams during its audits were valid and appropriate.

Calvin J. Rogers

President and Chief Executive Officer

James C. Watts

Senior Vice President and Chief Financial Officer

Report of Independent Registered Public Accounting Firm

To the shareholders and the board of directors of EarthWear Clothiers

Opinion on Internal Control over Financial Reporting

We have audited EarthWear Clothiers' internal control over financial reporting as of December 31, 2018, based on criteria established in *Internal Control—Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on criteria established in *Internal Control—Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"), the consolidated financial statements of EarthWear Clothiers, and our report dated February 15, 2019, expressed an unqualified opinion.

Basis for Opinion

The Company's management is responsible maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects.

Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinion.

Definition and Limitations of Internal Control Over Financial Reporting

A company's internal control over financial reporting is a process designed 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Willis & Adams

Boise, Idaho
February 15, 2019

Report of Independent Registered Public Accounting Firm

To the shareholders and the board of directors of EarthWear Clothiers

Opinion on the Financial Statements

We have audited the consolidated balance sheets of EarthWear Clothiers (the "Company") as of December 31, 2018 and 2017, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2018, and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the PCAOB, EarthWear Clothier's internal control over financial reporting as of December 31, 2018, based on the criteria established in *Internal Control—Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated February 15, 2019 expressed an unqualified opinion.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Critical Audit Matter

The critical audit matter communicated below is a matter arising from the current period audit of the financial statements that was communicated or required to be communicated to the audit committee and that: (1) relates to accounts or disclosures that are material to the financial statements and (2) involved especially challenging, subjective, or complex audit judgments. The communication of critical audit matters does not alter in any way our opinion on the financial statements, taken as a whole, and we are not, by communicating the critical audit matter below, providing separate opinions on the critical audit matter or on the accounts or disclosures to which it relates.

Critical Audit Matter	Auditor Response
IT systems and controls We place a high level of reliance on the Company's IT systems and key internal controls. As a result, a significant proportion of our audit effort was conducted in this area at local, regional and international levels and at the company's shared service centers. Our focus was on understanding and validating the impacts of key changes being made to the control environment. As indicated in EarthWear's financial statement disclosures, the Company has continued to devote considerable resources to the development of key business and related IT controls to ensure a robust system of internal control.	We conducted detailed end-to-end walkthroughs of the finance processes, utilizing our understanding from the prior year to reassess the design effectiveness of the key internal controls and to identify changes. We then conducted testing of the operating effectiveness of these controls to obtain evidence that they operated throughout the year. In response to the changes and control enhancements made during the year, we performed the following: • reviewed the design of the standard controls to ensure they mitigated the relevant financial reporting risks and testing samples from the periods immediately prior to and post implementation; • where systems changed during the year, tested IT general controls and data migration processes; • tested the enhanced user access management controls; and • tested controls and performed additional substantive procedures of key general ledger account reconciliations and manual journals.

Willis & Adams

Willis & Adams, CPAs

We have served as the Company's auditor since 1975.

Boise, Idaho
February 15, 2019