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 September 30, 2019

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: 001-31321

NAUTILUS, INC.
(Exact name of Registrant as specified in its charter)

Washington	**94-3002667**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

17750 S.E. 6th Way
Vancouver, Washington 98683
(Address of principal executive offices, including zip code)

(360) 859-2900
(Registrant's telephone number, including area code)

N/A
(Former name, former address and former fiscal year, if changed since last report)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, no par value	NLS	New York Stock Exchange

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 [x] 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [x] No [ ]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	[ ]	Accelerated filer	[x]	Non-accelerated filer	[ ]	Smaller reporting company	☒	Emerging growth company	☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. [ ]

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

The number of shares outstanding of the registrant's common stock as of October 31, 2019 was 29,728,321 shares.

NAUTILUS, INC.
FORM 10-Q
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2019

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

NAUTILUS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited and in thousands)

	As of	
	September 30, 2019	December 31, 2018
Assets		
Cash and cash equivalents	$ 5,756	$ 38,125
Available-for-sale securities	—	25,392
Trade receivables, net of allowances of $45 and $99	30,860	45,847
Inventories	50,066	68,465
Prepaids and other current assets	6,152	7,980
Income taxes receivable	2,747	5,653
Total current assets	95,581	191,462
Property, plant and equipment, net	22,366	22,216
Operating lease right-of-use assets	21,640	—
Goodwill	—	63,452
Other intangible assets, net	44,054	55,240
Other assets	4,498	574
Total assets	$ 188,139	$ 332,944
Liabilities and Shareholders' Equity		
Trade payables	$ 38,497	$ 87,265
Accrued liabilities	7,460	8,370
Operating lease liabilities, current portion	3,695	—
Warranty obligations, current portion	2,982	3,213
Note payable, current portion, net of unamortized debt issuance costs of $0 and $7	—	15,993
Total current liabilities	52,634	114,841
Operating lease liabilities, non-current	19,926	—
Warranty obligations, non-current	2,391	2,362
Income taxes payable, non-current	3,695	3,427
Deferred income tax liabilities, non-current	4,661	11,888
Other non-current liabilities	74	1,837
Debt payable, non-current, net of unamortized debt issuance costs of $256 and $7	20,296	15,993
Total liabilities	103,677	150,348
Commitments and contingencies (Note 18)		
Shareholders' equity:		
Common stock - no par value, 75,000 shares authorized, 29,728 and 29,545 shares issued and outstanding	625	215
Retained earnings	84,940	183,290
Accumulated other comprehensive loss	(1,103)	(909)
Total shareholders' equity	84,462	182,596
Total liabilities and shareholders' equity	$ 188,139	$ 332,944

See accompanying Notes to Condensed Consolidated Financial Statements.

NAUTILUS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited and in thousands, except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Net sales	$ 61,708	$ 91,057	$ 205,112	$ 281,368
Cost of sales	42,641	52,551	132,686	150,343
Gross profit	19,067	38,506	72,426	131,025
Operating expenses:				
Selling and marketing	17,472	20,635	69,146	79,482
General and administrative	6,726	7,503	23,824	20,740
Research and development	3,122	4,208	11,282	12,744
Goodwill and intangible impairment charge	—	—	72,008	—
Total operating expenses	27,320	32,346	176,260	112,966
Operating (loss) income	(8,253)	6,160	(103,834)	18,059
Other (expense) income:				
Interest income	—	269	162	835
Interest expense	(293)	(244)	(721)	(805)
Other, net	(129)	188	(351)	206
Total other (expense) income, net	(422)	213	(910)	236
(Loss) income from continuing operations before income taxes	(8,675)	6,373	(104,744)	18,295
Income tax expense (benefit)	1,900	1,870	(6,941)	4,645
(Loss) income from continuing operations	(10,575)	4,503	(97,803)	13,650
Discontinued operations:				
Loss from discontinued operations before income taxes	(39)	(159)	(104)	(187)
Income tax expense of discontinued operations	75	35	225	167
Loss from discontinued operations	(114)	(194)	(329)	(354)
Net (loss) income	$ (10,689)	$ 4,309	$ (98,132)	$ 13,296
Basic (loss) income per share from continuing operations	$ (0.36)	$ 0.15	$ (3.30)	$ 0.45
Basic loss per share from discontinued operations	—	(0.01)	(0.01)	(0.01)
Basic net (loss) income per share	$ (0.36)	$ 0.14	$ (3.31)	$ 0.44
Diluted (loss) income per share from continuing operations	$ (0.36)	$ 0.15	$ (3.30)	$ 0.45
Diluted loss per share from discontinued operations	—	(0.01)	(0.01)	(0.01)
Diluted net (loss) income per share	$ (0.36)	$ 0.14	$ (3.31)	$ 0.44
Shares used in per share calculations:				
Basic	29,728	30,185	29,660	30,230
Diluted	29,728	30,433	29,660	30,500

See accompanying Notes to Condensed Consolidated Financial Statements.

NAUTILUS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME
(Unaudited and in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	**2018**	**2019**	**2018**
Net (loss) income	$ (10,689)	$ 4,309	$ (98,132)	$ 13,296
Other comprehensive (loss) income:				
Unrealized gain (loss) on available-for-sale securities, net of income tax expense of $0, $13, $6 and $6	—	40	6	37
(Loss) gain on derivative securities, effective portion, net of income tax expense (benefit) of $0, $(6), $(139) and $26	—	(18)	(223)	138
Foreign currency translation, net of income tax (benefit) expense of $(37), $7, $(101) and $7	(177)	82	23	(373)
Other comprehensive (loss) income	(177)	104	(194)	(198)
Comprehensive (loss) income	$ (10,866)	$ 4,413	$ (98,326)	$ 13,098

See accompanying Notes to Condensed Consolidated Financial Statements.

NAUTILUS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(Unaudited and in thousands)

	Common Stock			Accumulated Other Comprehensive (Loss) Income	
	Shares	Amount	Retained Earnings		Total Shareholders' Equity
Balances at December 31, 2018	29,545	$ 215	$ 183,290	$ (909)	$ 182,596
Net loss	—	—	(8,575)	—	(8,575)
Unrealized gain on marketable securities, net of income tax expense of $5	—	—	—	15	15
Loss on derivative securities, effective portion, net of income tax benefit of $33	—	—	—	(100)	(100)
Foreign currency translation adjustment, net of income tax benefit of $55	—	—	—	128	128
Stock-based compensation expense	—	(147)	(218)	—	(365)
Common stock issued under equity compensation plan, net of shares withheld for tax payments	48	(68)	—	—	(68)
Balances at March 31, 2019	29,593	—	174,497	(866)	173,631
Net loss	—	—	(78,868)	—	(78,868)
Unrealized loss on marketable securities, net of income tax expense of $1	—	—	—	(9)	(9)
Loss on derivative securities, effective portion, net of income tax benefit of $106	—	—	—	(123)	(123)
Foreign currency translation adjustment, net of income tax benefit of $9	—	—	—	72	72
Stock-based compensation expense	—	9	—	—	9
Common stock issued under equity compensation plan, net of shares withheld for tax payments	87	36	—	—	36
Common stock issued under employee stock purchase plan	48	168	—	—	168
Balances at June 30, 2019	29,728	213	95,629	(926)	94,916
Net loss	—	—	(10,689)	—	(10,689)
Foreign currency translation adjustment, net of income tax benefit of $37	—	—	—	(177)	(177)
Stock-based compensation expense	—	412	—	—	412
Balances at September 30, 2019	29,728	$ 625	$ 84,940	$ (1,103)	$ 84,462

NAUTILUS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(Unaudited and in thousands)

	Common Stock				
	Shares	Amount	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Total Shareholders' Equity
Balances at December 31, 2017	30,305	$ —	$ 179,448	$ (259)	$ 179,189
Net income	—	—	8,059	—	8,059
Unrealized loss on marketable securities, net of income tax benefit of $18	—	—	—	(37)	(37)
Gain on derivative securities, effective portion, net of income tax expense of $28	—	—	—	144	144
Foreign currency translation adjustment, net of income tax benefit of $3	—	—	—	(117)	(117)
Stock-based compensation expense	—	479	—	—	479
Common stock issued under equity compensation plan, net of shares withheld for tax payments	67	(99)	—	—	(99)
Repurchased shares	(211)	(150)	(2,568)	—	(2,718)
Balances at March 31, 2018	30,161	230	184,939	(269)	184,900
Net income	—	—	928	—	928
Unrealized gain on marketable securities, net of income tax expense of $11	—	—	—	34	34
Gain on derivative securities, effective portion, net of income tax expense of $4	—	—	—	12	12
Foreign currency translation adjustment, net of income tax expense of $3	—	—	—	(338)	(338)
Stock-based compensation expense	—	268	—	—	268
Common stock issued under equity compensation plan, net of shares withheld for tax payments	87	(198)	—	—	(198)
Common stock issued under employee stock purchase plan	20	232	—	—	232
Repurchased shares	(31)	(70)	(178)	—	(248)
Balances at June 30, 2018	30,237	462	185,689	(561)	185,590
Net income	—	—	4,309	—	4,309
Unrealized gain on marketable securities, net of income tax expense of $13	—	—	—	40	40
Loss on derivative securities, effective portion, net of income tax benefit of $6	—	—	—	(18)	(18)
Foreign currency translation adjustment, net of income tax expense of $7	—	—	—	82	82
Stock-based compensation expense	—	647		—	647
Common stock issued under equity compensation plan, net of shares withheld for tax payments	28	78	—	—	78
Repurchased shares	(134)	(971)	(891)	—	(1,862)
Balances at September 30, 2018	30,131	$ 216	$ 189,107	$ (457)	$ 188,866

See accompanying Notes to Condensed Consolidated Financial Statements.

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NAUTILUS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited and in thousands)

	Nine Months Ended September 30,	
	2019	**2018**
Cash flows from operating activities:		
(Loss) income from continuing operations	$ (97,803)	$ 13,650
Loss from discontinued operations	(329)	(354)
Net (loss) income	(98,132)	13,296
Adjustments to reconcile net (loss) income to cash (used in) provided by operating activities:		
Depreciation and amortization	8,045	6,646
Provision (benefit) for allowance for doubtful accounts	52	(42)
Inventory lower-of-cost-or-market/NRV adjustments	692	255
Stock-based compensation expense	56	1,394
Loss on asset dispositions	1,127	32
Goodwill and intangible impairment charge	72,008	—
Deferred income taxes, net of valuation allowance of $5,083 and $1,045	(7,456)	1,476
Other	(115)	40
Changes in operating assets and liabilities:		
Trade receivables	15,079	(3,352)
Inventories	18,284	(2,503)
Prepaids and other assets	4,168	1,075
Income taxes receivable	2,906	(4,712)
Trade payables	(48,973)	(525)
Accrued liabilities and other liabilities, including warranty obligations	(3,325)	(3,254)
Net cash (used in) provided by operating activities	(35,584)	9,826
Cash flows from investing activities:		
Purchases of available-for-sale securities	—	(29,522)
Proceeds from sales and maturities of available-for-sale securities	25,271	46,475
Purchases of property, plant and equipment	(6,630)	(6,557)
Proceeds from sale of property, plant and equipment	—	4
Purchases of other investments in non-controlled affiliates	(3,500)	—
Net cash provided by investing activities	15,141	10,400
Cash flows from financing activities:		
Proceeds from long-term debt	20,218	—
Payments on long-term debt	(31,667)	(12,000)
Payments for stock repurchases	—	(4,989)
Proceeds from employee stock purchases	168	232
Proceeds from exercise of stock options	75	338
Tax payments related to stock award issuances	(107)	(396)
Net cash used in financing activities	(11,313)	(16,815)
Effect of exchange rate changes on cash and cash equivalents	(613)	(551)
(Decrease) increase in cash and cash equivalents	(32,369)	2,860
Cash and cash equivalents:		
Beginning of period	38,125	27,893
End of period	$ 5,756	$ 30,753
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 963	$ 799
Cash (received) paid for income taxes, net	(2,203)	8,622
Supplemental disclosure of non-cash investing activities:		
Capital expenditures incurred but not yet paid	$ 415	$ 1,352

See accompanying Notes to Condensed Consolidated Financial Statements.

NAUTILUS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(1) GENERAL INFORMATION

Basis of Consolidation and Presentation

The accompanying condensed consolidated financial statements present the financial position, results of operations and cash flows of Nautilus, Inc. and its subsidiaries, all of which are wholly owned. Intercompany transactions and balances have been eliminated in consolidation.

The accompanying condensed consolidated financial statements have not been audited. We have condensed or omitted certain information and footnote disclosures normally included in financial statements presented in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"). Management believes the disclosures contained herein are adequate to make the information presented not misleading. However, these condensed consolidated financial statements should be read in conjunction with our consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2018 (the "2018 Form 10-K").

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. Further information regarding significant estimates can be found in our 2018 Form 10-K.

In the opinion of management, the accompanying condensed consolidated financial statements reflect all adjustments necessary to present fairly our financial position as of September 30, 2019 and December 31, 2018, and our results of operations, comprehensive (loss) income and shareholders' equity for the three and nine months ended September 30, 2019 and 2018 and our cash flows for the nine months ended September 30, 2019 and 2018. Interim results are not necessarily indicative of results for a full year. Our revenues typically vary seasonally, and this seasonality can have a significant effect on operating results, inventory levels and working capital needs.

Unless indicated otherwise, all information regarding our operating results pertain to our continuing operations.

Recent Accounting Pronouncements

<u>*Recently Adopted Pronouncements*</u>

ASUs 2018-11, 2018-10, 2018-01 and 2016-02

In February 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-02, "Leases (Topic 842)." ASU 2016-02 replaces the existing guidance in Accounting Standards Codification ("ASC") 840, Leases. The new standard requires lessees to recognize leases on-balance sheet and disclose key information about leasing arrangements. Topic 842 was subsequently amended by ASU 2018-01, "Land Easement Practical Expedient for Transition to Topic 842"; ASU 2018-10, "Codification Improvements to Topic 842, Leases;" and ASU 2018-11, "Targeted Improvements." The new standard establishes a right-of-use model ("ROU") that requires a lessee to recognize a ROU asset and lease liability on the balance sheet for all leases with a term longer than 12 months. Leases will be classified as finance or operating. For finance leases, the lessee recognizes interest expense and amortizes the ROU asset, and, for operating leases, the lessee recognizes lease expense on a straight-line basis.

The new standard was effective for us on January 1, 2019. A modified retrospective transition approach was required, applying the new standard to all leases existing at the date of initial application. An entity may choose to use either (1) its effective date or (2) the beginning of the earliest comparative period presented in the financial statements as its date of initial application. We adopted the new standard on January 1, 2019 and used the effective date as our date of initial application. Consequently, financial information was not updated and the disclosures required under the new standard were not provided for dates and periods prior to January 1, 2019.

The new standard provides a number of optional practical expedients in transition. We elected the 'package of practical expedients,' which permitted us not to reassess, under the new standard, our prior conclusions about lease identification, lease classification, and initial direct costs. We elected the use-of-hindsight with respect to determining lease terms. We did not elect the practical expedient pertaining to land easements as it is not applicable to us.

The new standard also provides practical expedients for an entity's ongoing accounting. We elected the short-term lease recognition exemption for all leases that qualified. This means, for those leases that qualify, we did not recognize ROU assets or lease liabilities, and this includes not recognizing ROU assets or lease liabilities for existing short-term leases of those assets in transition. Variable payments, including payments for the Company's proportionate share of the building's property taxes, insurance, and common area maintenance, are treated as non-lease components and are recognized in earnings in the period for which the costs occur.

The new standard had a material effect on our financial statements with the most significant effects relating to the recognition of new ROU assets and lease liabilities on our balance sheet for our facilities operating leases, and providing significant new disclosures about our leasing activities.

We reviewed our existing vendor contracts for potential embedded leases, as well as renewal options and whether exercises of renewal options were reasonably certain. Based on our analyses of our existing operating and financing leases, we recognized additional operating lease liabilities of approximately $25 million, with corresponding ROU assets of the same amount based on the present value of the remaining minimum lease payments under current leasing standards for existing operating leases, net of reductions for the impacts of deferred rents and lease incentives. The additional disclosures required by the ASU are included in Note 9, *Leases*.

ASU 2018-09
In July 2018, the FASB issued ASU 2018-09, "Codification Improvements." The FASB has a standing project to address suggestions received from stakeholders on the ASC and to make other incremental improvements to GAAP. This perpetual project facilitates ASC updates for technical corrections, clarifications, and other minor improvements, and these amendments are referred to as Codification improvements. ASU 2018-09 includes amendments affecting a wide variety of topics and applies to all reporting entities within the scope of the affected accounting guidance. The transition and effective date guidance is based on the facts and circumstances of each amendment. Some of the amendments in the ASU do not require transition guidance and are effective upon issuance of the ASU. However, many of the amendments in the ASU have transition guidance with effective dates for annual periods beginning after December 15, 2018, for public business entities. Our adoption of ASU 2018-09 as of January 1, 2019 had no material impact on our financial position, results of operations or cash flows.

ASU 2018-07
In June 2018, the FASB issued ASU 2018-07, "Compensation - Stock Compensation (Topic 718) - Improvements to Nonemployee Share-Based Payment Accounting." ASU 2018-07 expands the scope of Topic 718 to include share-based payment transactions for acquiring goods and services from nonemployees. An entity should apply the requirements of Topic 718 to nonemployee awards with certain exceptions. ASU 2018-07 specifies that Topic 718 applies to all share-based payment transactions in which a grantor acquires goods or services to be used or consumed in a grantor's own operations by issuing share-based payment awards. Further, Topic 718 does not apply to share-based payments used to effectively provide (1) financing to the issuer or (2) awards granted in conjunction with selling goods or services to customers as part of a contract accounted for under Topic 606, *Revenue from Contracts with Customers*. ASU 2018-07 is effective for public companies' fiscal years, including interim periods within those fiscal years, beginning after December 15, 2018. Our adoption of ASU 2018-07 as of January 1, 2019 had no material impact on our financial position, results of operations or cash flows.

ASU 2018-02
In February 2018, the FASB issued ASU 2018-02, "Income Statement - Reporting Comprehensive Income (Topic 220)." ASU 2018-02 allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the TCJA, thereby eliminating the stranded tax effects and improving the usefulness of reported information to financial statement users. ASU 2018-02 is effective for all entities for fiscal years, including interim periods within those fiscal years, beginning after December 15, 2018. Early adoption is permitted, including adoption in any interim period, for public business entities for which financial statements have not yet been issued. Our adoption of ASU 2018-02 as of January 1, 2019 had no material impact on our financial position, results of operations or cash flows.

ASU 2017-12
In August 2017, the FASB issued ASU 2017-12, "Derivatives and Hedging (Topic 815) - Targeted Improvements to Accounting for Hedging Activities." ASU 2017-12 provides better alignment of an entity's risk management activities and financial reporting of hedges through changes to both the designation and measurement guidance for qualifying hedging relationships. In addition, the amendments in ASU 2017-12 also simplify the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements to increase the understandability of the results of an entity's intended hedging strategies. ASU 2017-12 is effective for public companies' fiscal years, including interim periods within those fiscal years, beginning after

December 15, 2018. For cash flow and net investment hedges existing as of the adoption date, an entity should apply a cumulative-effect adjustment related to eliminating the separate measurement of ineffectiveness to accumulated other comprehensive income and opening retaining earnings. Amended presentation and disclosure guidance is required only prospectively, and certain transition elections are available upon adoption. Our adoption of ASU 2017-12 as of January 1, 2019 had no material impact on our financial position, results of operations or cash flows.

Recently Issued Pronouncements Not Yet Adopted

ASU 2019-01
In March 2019, the FASB issued ASU 2019-01, "Leases (Topic 842): Codification Improvements." The amendments in ASU 2019-01 address three issues (1) determining the fair value of the underlying asset by lessors that are not manufactures or dealers; (2) presentation on the statement of cash flows of sales-type and direct financing leases; and (3) transition disclosures related to Topic 250, Accounting Changes and Error Corrections. ASU 2019-01 is effective for public companies' fiscal years, including interim periods within those fiscal years, beginning after December 15, 2019 with early application permitted. While we do not expect the adoption of ASU 2019-01 to have a material effect on our business, we are evaluating the potential impact that ASU 2019-01 may have on our financial position, results of operations and cash flows.

ASU 2018-15
In August 2018, the FASB issued ASU 2018-15, "Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract." The amendments in ASU 2018-15 align the requirements for capitalizing implementation costs incurred in a cloud computing hosting arrangement ("CCA") that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. The accounting for the service element of a hosting arrangement that is a service contract is not affected. ASU 2018-15 also includes provisions for expensing the capitalized implementation costs over the term of the hosting arrangement, and application of impairment and abandonment guidance under Subtopics 350-40 and 360-10, respectively. Further, the amendments include presentation requirements in the entity's financial statements for the capitalized implementation costs and related amortization expense. ASU 2018-15 is effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Early adoption is permitted, and the amendments should be applied either retrospectively or prospectively to all implementation costs incurred after the date of adoption. We expect to have presentation changes to our consolidated balance sheets, otherwise, we do not expect the adoption of ASU 2018-15 to have a material impact to our financial statements or to our business processes.

ASU 2018-13
In August 2018, the FASB issued ASU 2018-13, "Fair Value Measurement (Topic 820): Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement." The amendments in ASU 2018-13 modify the disclosure requirements on fair value measurements in Topic 820 based on the concepts in the FASB Concepts Statement, *Conceptual Framework for Financial Reporting - Chapter 8: Notes to Financial Statements*, which was finalized in August 2018. The main provisions include removals, modifications, and additions of specific disclosure requirements. ASU 2018-13 is effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Certain amendments should be applied prospectively for only the most recent interim or annual period presented in the initial year of adoption, while all other amendments should be applied retrospectively to all periods presented upon their effective date. Early adoption is permitted, and an entity may early adopt upon issuance of ASU 2018-13 those amendments that remove or modify disclosures and delay adoption of the additional disclosures until the effective date. While we do not expect the adoption of ASU 2018-13 to have a material effect on our business, we are evaluating the potential impact that the new ASU may have on our financial position, results of operations and cash flows.

ASU 2016-13
In June 2016, the FASB issued ASU 2016-13, "Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." ASU 2016-13 requires companies to measure credit losses utilizing a methodology that reflects expected credit losses and requires a consideration of a broader range of reasonable and supportable information to inform credit loss estimates. ASU 2016-13 is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. We are currently assessing the impact of adopting this standard but do not expect the adoption of this guidance to have a material impact on our financial position, results of operations and cash flows.

(2) REVENUES

Revenue Recognition
Revenues are recognized when control of the promised goods or services is transferred to our customers, in an amount that reflects the consideration we expect to be entitled to in exchange for those goods or services. Our product sales and shipping revenues are reported net of promotional discounts, returns allowances, contractual rebates, and consideration payable to our customers. We

estimate the revenue impact of retail sales incentive programs based on the planned duration of the program and historical experience. If the amount of sales incentives is reasonably estimable, the impact of such incentives is recorded at the later of the time the customer is notified of the sales incentive or the time of the sale. We estimate our liability for product returns based on historical experience, and record the expected customer refund liability as a reduction of revenue, and the expected inventory right of recovery, net of estimated scrap, as a reduction of cost of sales. If actual return costs differ from previous estimates, the amount of the liability and corresponding revenue are adjusted in the period in which such costs occur.

We provide standard assurance-type warranties on our products which cover defective materials or nonconforming products, and is included with each product at no additional charge. In addition, we offer service-type/extended warranties for an additional fee to our Direct channel customers and Retail specialty and commercial customers. These warranty contracts provide coverage on labor and parts beyond the standard assurance warranty period.

For our product sales, services, and freight and delivery fees, we are the principal in the contract and recognize revenue at a point in time. For our Direct channel extended warranty contracts, we are the agent and recognize revenue on a net basis because our performance obligation is to facilitate the arrangement between our customers and the third-party performance obligor.

For customer contracts that include multiple performance obligations, we allocate revenue to each performance obligation based on its relative standalone selling price. We generally determine standalone selling price based on prices charged to customers or using expected cost plus margin.

Our revenues from contracts with customers disaggregated by revenue source, excluding sales-based taxes, were as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Product sales	$ 59,323	$ 88,068	$ 195,781	$ 269,288
Extended warranties and services	993	1,611	4,630	6,830
Other[(1)]	1,392	1,378	4,701	5,250
Net sales	$ 61,708	$ 91,057	$ 205,112	$ 281,368

[(1)] Other revenue is primarily freight and delivery, royalty income and subscription revenue.

Our revenues disaggregated by geographic region, based on ship-to address, were as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
United States	$ 50,447	$ 81,423	$ 169,532	$ 250,502
Canada	5,649	4,306	17,135	13,372
All other	5,612	5,328	18,445	17,494
Net sales	$ 61,708	$ 91,057	$ 205,112	$ 281,368

As of September 30, 2019, estimated revenue expected to be recognized in the future totaled $5.9 million, primarily related to customer order backlog, which includes firm orders for future shipment to our Retail customers, as well as unfulfilled consumer orders within the Direct channel. Retail orders of $5.3 million and Direct orders of $0.6 million comprised our backlog as of September 30, 2019. The estimated future revenues are net of contractual rebates and consideration payable for applicable Retail customers, and net of current promotional programs and sales discounts for our Direct customers.

The following table provides information about our liabilities from contracts with customers, primarily customer deposits and deferred revenue, all of which are short-term in nature. The revenue recognized from contract liabilities and the remaining balances are presented in accrued liabilities and are shown below (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Balance, beginning of period	$ 562	$ 748	$ 816	$ 1,084
Cash additions	611	354	1,123	1,347
Revenue recognition	(279)	(227)	(1,045)	(1,556)
Balance, end of period	$ 894	$ 875	$ 894	$ 875

Exemptions and Elections

We apply the practical expedient as per ASC 606-10-50-14 and do not disclose information related to remaining performance obligations due to their original expected durations are one year or less.

We expense sales commissions when incurred because the amortization period would have been less than one year. These costs are recorded in selling and marketing expense.

We generally account for our shipping and handling activities as a fulfillment activity, consistent with the timing of revenue recognition; that is, when our customer takes control of the transferred goods. In the event that a customer were to take control of a product prior to shipment, we make an accounting policy election to treat such shipping and handling activities as a fulfillment cost.

(3) INVESTMENTS

During the nine months ended September 30, 2019, we made strategic equity securities investments to increase our digital capabilities. Effective January 1, 2018, we adopted ASU Financial Instruments—Overall: Recognition and Measurement of Financial Assets and Financial Liabilities, which requires us to measure all equity investments that do not result in consolidation and are not accounted for under the equity method at fair value and recognize any changes in earnings. We use quoted market prices to determine the fair values of equity securities with readily determinable fair values. For equity securities without readily determinable fair values, we have elected the measurement alternative under which we measure these investments at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer. Management assesses each of these investments on an individual basis.

The accounting guidance related to the classification and measurement of certain equity investments requires us to account for these investments at fair value or to elect to account for these investments under the "practicability exception," which permits measurement of these investments at cost, minus impairments, plus or minus observable changes in price for each reporting period. As of September 30, 2019, we had elected the practicability exception for equity investments without readily determinable fair values of $3.5 million and have not recognized any impairments or any upward adjustments on either an annual or cumulative basis due to observable price changes.

As of September 30, 2019, the carrying values of our equity securities were included in the following line item in our consolidated balance sheets (in thousands):

	Measurement Alternative - No Readily Determinable Fair Value
Other assets	$ 3,500

(4) FAIR VALUE MEASUREMENTS

Factors used in determining the fair value of financial assets and liabilities are summarized into three broad categories:

- Level 1 - observable inputs such as quoted prices (unadjusted) in active liquid markets for identical securities as of the reporting date;

- Level 2 - other significant directly or indirectly observable inputs, including quoted prices for similar securities, interest rates, prepayment speeds and credit risk; or observable market prices in markets with insufficient volume and/or infrequent transactions; and
- Level 3 - significant inputs that are generally unobservable inputs for which there is little or no market data available, including our own assumptions in determining fair value.

Assets and liabilities measured at fair value on a recurring basis were as follows (in thousands):

	September 30, 2019			
	Level 1	Level 2	Level 3	Total
Liabilities:				
Derivatives				
Foreign currency forward contracts	$ —	$ 218	$ —	$ 218
Total liabilities measured at fair value	$ —	$ 218	$ —	$ 218

	December 31, 2018			
	Level 1	Level 2	Level 3	Total
Assets:				
Cash Equivalents				
Money market funds	$ 7,646	$ —	$ —	$ 7,646
Total cash equivalents	7,646	—	—	7,646
Available-for-Sale Securities				
Certificates of deposit[(1)]	—	10,379	—	10,379
Corporate bonds	—	7,522	—	7,522
U.S. government bonds	—	7,491	—	7,491
Total available-for-sale securities	—	25,392	—	25,392
Derivatives				
Interest rate swap contract	—	363	—	363
Foreign currency forward contracts	—	240	—	240
Total derivatives	—	603	—	603
Total assets measured at fair value	$ 7,646	$ 25,995	$ —	$ 33,641

[(1)] All certificates of deposit are within current FDIC insurance limits.

We did not have any assets measured at fair value on a recurring basis as of September 30, 2019 and liabilities measured at fair value on a recurring basis as of December 31, 2018.

For our assets measured at fair value on a recurring basis, we recognize transfers between levels at the actual date of the event or change in circumstance that caused the transfer. There were no transfers between levels during the nine months ended September 30, 2019, nor for the year ended December 31, 2018.

We did not have any changes to our valuation techniques during the nine months ended September 30, 2019, nor for the year ended December 31, 2018.

We classify our marketable securities as available-for-sale and, accordingly, record them at fair value. Level 1 investment valuations are obtained from real-time quotes for transactions in active exchange markets involving identical assets. Level 2 investment valuations are obtained from inputs, other than quoted market prices in active markets for identical assets, that are directly or indirectly observable in the marketplace and quoted prices in markets with limited volume or infrequent transactions. The factors or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities. Unrealized holding gains and losses are excluded from earnings and are reported net of tax in comprehensive income until realized.

The fair values of our interest rate swap contract and our foreign currency forward contracts are calculated as the present value of estimated future cash flows using discount factors derived from relevant Level 2 market inputs, including forward curves and volatility levels.

We recognize or disclose the fair value of certain assets, such as non-financial assets, primarily property, plant and equipment, goodwill, other intangible assets and certain other long-lived assets in connection with impairment evaluations. All of our nonrecurring valuations use significant unobservable inputs and therefore fall under Level 3 of the fair value hierarchy.

ASC 350 — Intangibles — *Goodwill and Other*, requires us to make significant assumptions and estimates about the extent and timing of future cash flows, discount rates, growth rates and terminal value. The cash flows are estimated over a significant future period of time, which makes those estimates and assumptions subject to an even higher degree of uncertainty. We also use market valuation models and other financial ratios, which require us to make certain assumptions and estimates regarding the applicability of those models to our assets and businesses.

We perform a goodwill and indefinite-lived asset impairment evaluation during the fourth quarter of each year. However, as a result of the decline in our market value relative to the market and our industry, identified as a triggering event, we performed an interim Step 1 evaluation and a market capitalization reconciliation during the second quarter of 2019.

The goodwill evaluation was performed using a quantitative assessment at each reporting unit level and we determined that is was more-likely-than-not that the fair value of goodwill assigned to our reporting units was less than the carrying amount. We assigned assets and liabilities to each reporting unit based on either specific identification or by using judgment for the remaining assets and liabilities that are not specific to a reporting unit. We determined the fair value of our reporting units in Step 1 of the ASC 350 analysis using the income approach and the market approach. In addition, we determined the fair value by adding a control premium observed from recent transactions of comparable companies to determine the reasonableness of that assumption and the fair values of the reporting units estimated in Step 1. Significant unobservable inputs and assumptions inherent in the valuation methodologies from Level 3 inputs were employed and include, but were not limited to, prospective financial information, growth rates, terminal value, royalty rates, discount rates, and comparable multiples from publicly traded companies in our industry. We compared the carrying amount of each reporting unit to its respective fair value. We reconciled the aggregate fair values of the reporting units determined in Step 1 (as described above) to the enterprise market capitalization plus a reasonable control premium. We determined both reporting units were impaired and recorded a $63.5 million non-cash goodwill impairment.

The indefinite-lived intangible assets evaluation was performed using the relief from royalty method during the second quarter of 2019. This analysis was based on the estimated future cash flows generated for each separate brand/trademark. We compared the carrying amount to the estimated fair values. Based on our evaluation, the Octane trademark with a carrying value of $14.2 million was written down to its fair value of $5.7 million, resulting in an $8.5 million non-cash intangible asset impairment.

During the year ended December 31, 2018, there were no assets or liabilities that were recorded at fair value on a nonrecurring basis.

The carrying values of cash and cash equivalents, trade receivables, prepaids and other current assets, trade payables and accrued liabilities approximate fair value due to their short maturities. The carrying value of our debt approximates its fair value and falls under Level 2 of the fair value hierarchy, as the interest rate is variable and based on current market rates.

(5) DERIVATIVES

From time to time, we enter into interest rate swaps to fix a portion of our interest expense, and foreign exchange forward contracts to offset the earnings impacts of exchange rate fluctuations on certain monetary assets and liabilities. We do not enter into derivative instruments for any purpose other than to manage interest rate or foreign currency exposure. That is, we do not engage in interest rate or currency exchange rate speculation using derivative instruments.

As of June 30, 2019, we terminated a $20.0 million interest rate swap with JPMorgan Chase Bank, N.A. The termination of this interest rate swap discontinued the cash flow hedging relationship for our line of credit and had unrealized gains. As of June 30, 2019, we reclassified $0.1 million, net of tax, of unrealized gains from accumulated other comprehensive losses to other income.

We may hedge our net recognized foreign currency assets and liabilities with forward foreign exchange contracts to reduce the risk that our earnings and cash flows will be adversely affected by changes in foreign currency exchange rates. These derivative instruments hedge assets and liabilities that are denominated in foreign currencies and are carried at fair value with changes in the fair value recorded as other income. These derivative instruments do not subject us to material balance sheet risk due to exchange rate movements because gains and losses on these derivatives are intended to offset gains and losses on the assets and liabilities being hedged. As of September 30, 2019, total outstanding contract notional amounts were $17.6 million. At September 30, 2019, these outstanding balance sheet hedging derivatives had maturities of 108 days or less.

The fair value of our derivative instruments was included in our condensed consolidated balance sheets as follows (in thousands):

	Balance Sheet Classification	As of September 30, 2019	As of December 31, 2018
Derivative instruments designated as cash flow hedges:			
Interest rate swap contract	Prepaids and other current assets	$ —	$ 291
	Other assets	—	72
		$ —	$ 363
Derivative instruments not designated as cash flow hedges:			
Foreign currency forward contracts	Prepaids and other current assets	$ —	$ 240
	Accrued liabilities	218	—
		$ 218	$ 240

The effect of derivative instruments on our condensed consolidated statements of operations was as follows (in thousands):

	Statement of Operations Classification	Three Months Ended September 30, 2019	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2019	Nine Months Ended September 30, 2018
Derivative instruments designated as cash flow hedges:					
Income (loss) recognized in other comprehensive (loss) income before reclassifications	---	$ —	$ 28	$ (128)	$ 242
Income reclassified from accumulated other comprehensive (loss) income to earnings for the effective portion	Interest expense	—	65	125	140
Income tax benefit	Income tax expense (benefit)	—	(19)	(30)	(36)
Derivative instruments not designated as cash flow hedges:					
Loss recognized in earnings	Other, net	$ (388)	$ (601)	$ (101)	$ (2,525)
Income tax expense	Income tax expense (benefit)	91	176	22	624

For additional information related to our derivatives, see Notes 4 and 12.

(6) INVENTORIES

Inventories are stated at the lower of cost and net realizable value, with cost determined based on the first-in, first-out method. Our inventories consisted of the following (in thousands):

	As of September 30, 2019	As of December 31, 2018
Finished goods	$ 44,542	$ 63,257
Parts and components	5,524	5,208
Total inventories	$ 50,066	$ 68,465

(7) PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consisted of the following (in thousands):

	Estimated Useful Life (in years)	As of September 30, 2019	As of December 31, 2018
Automobiles	5	$ 23	$ 23
Leasehold improvements	4 to 20	3,829	3,782
Computer software and equipment	2 to 7	24,903	23,776
Machinery and equipment	3 to 5	18,049	16,756
Furniture and fixtures	5 to 20	2,839	2,827
Work in progress[1]	N/A	3,019	1,590
Total cost		52,662	48,754
Accumulated depreciation		(30,296)	(26,538)
Total property, plant and equipment, net		$ 22,366	$ 22,216

[1] Work in progress includes information technology assets and production tooling.

Depreciation expense was as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Depreciation expense	$ 2,046	$ 1,393	$ 5,353	$ 4,266

(8) GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill

The rollforward of goodwill was as follows (in thousands):

	Direct	Retail	Total
Balance, January 1, 2018	$ 2,335	$ 59,695	$ 62,030
Currency exchange rate adjustment	(185)	5	(180)
Business acquisition	1,602	—	1,602
Balance, December 31, 2018	3,752	59,700	63,452
Currency exchange rate adjustment	55	—	55
Goodwill impairment charge	(3,807)	(59,700)	(63,507)
Balance, September 30, 2019	$ —	$ —	$ —

In accordance ASC 350 — Intangibles — *Goodwill and Other*, we perform a goodwill and indefinite-lived asset impairment evaluation during the fourth quarter of each year. However, as a result of the decline in our market value relative to the market and our industry, identified as a triggering event, we performed an interim evaluation and a market capitalization reconciliation during the second quarter of 2019, which resulted in a non-cash goodwill and indefinite-lived intangible assets impairment charge of $72.0 million, $63.5 million and $8.5 million respectively.

Other Intangible Assets

Other intangible assets consisted of the following (in thousands):

	Estimated Useful Life (in years)	As of September 30, 2019	As of December 31, 2018
Indefinite-lived trademarks[1]	N/A	$ 14,753	$ 23,252
Definite-lived trademarks	5 to 15	2,850	2,850
Patents	7 to 24	14,243	14,243
Customer relationships	10 to 15	24,700	24,700
		56,546	65,045
Accumulated amortization - definite-lived intangible assets		(12,492)	(9,805)
Other intangible assets, net		$ 44,054	$ 55,240

[1] During the second quarter of 2019, we identified impairment indicators with our indefinite-lived trademarks resulting in an $8.5 million non-cash intangible impairment charge.

Amortization expense was as follows (in thousands):

	Three Months Ended September 30, 2019	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2019	Nine Months Ended September 30, 2018
Amortization expense	$ 808	$ 785	$ 2,692	$ 2,380

Future amortization of definite-lived intangible assets is as follows (in thousands):

Remainder of 2019	$ 803
2020	3,198
2021	3,168
2022	3,168
2023	3,168
Thereafter	15,796
	$ 29,301

(9) LEASES

We have several noncancellable operating leases, primarily for office space, that expire at various dates over the next five years. These leases generally contain renewal options to extend for one lease term of five years. For leases that we are reasonably certain we will exercise the lease renewal options, the options were considered in determining the lease term, and associated potential option payments are included in the lease payments. The payments used in the renewal term were estimated using the percentage rate increase of historical rent payments for each location where the renewal will be exercised.

Payments due under the lease contracts include annual fixed payments for office space. Variable payments including payments for our proportionate share of the building’s property taxes, insurance, and common area maintenance are treated as non-lease components and are recognized in the period for which the costs occur.

The components of lease cost were as follows (in thousands):

	Three Months Ended September 30, 2019	Nine Months Ended September 30, 2019
Operating lease expense	$ 1,138	$ 3,393

Leases with an initial term of 12 months or less ("short-term lease") are not recorded on the balance sheet and are recognized on a straight-line basis over the lease term. The short-term lease expense for the three and nine months ended September 30, 2019 was $30 thousand and $242 thousand, respectively.

Other information related to leases was as follows (dollars in thousands):

		As of September 30, 2019
Supplemental cash flow information:		
Cash paid for amounts included in the measurement of operating lease liabilities:		
Operating cash flow from operating leases	$	3,415
Additional operating lease information:		
ROU assets obtained in exchange for operating lease obligations	$	24,212
Reductions to ROU assets resulting from reductions to operating lease obligations	$	2,572
Weighted average remaining operating lease term	4.0 years	
Weighted average discount rate on operating leases		4.49%

Amounts disclosed for ROU assets obtained in exchange for lease obligations include amounts added to the carrying amount of ROU assets resulting from lease modifications and reassessments including transition liabilities upon adoption of ASC 842 on January 1, 2019. We determined the discount rate for leases using an incremental borrowing rate to calculate the ROU assets and lease liabilities.

Maturities of operating lease liabilities under noncancellable leases were as follows (in thousands):

		As of September 30, 2019
2019 - remaining	$	1,164
2020		4,682
2021		4,712
2022		4,566
2023		3,812
Thereafter		8,082
Total undiscounted lease payments		27,018
Less imputed interest		(3,397)
Total lease liabilities	$	23,621

Under ASC 840, *Leases,* future minimum lease payments under noncancellable operating leases payments were as follows (in thousands):

		As of December 31, 2018
Year ending:		
2019	$	5,366
2020		5,279
2021		4,147
2022		2,729
2023		1,698
Thereafter		2,647
Total minimum lease payments	$	21,866

Minimum rental lease payments under operating leases are recognized on a straight-line basis over the term of the lease including any periods of rent abatement and incentives. Rental expense for operating leases for the three and nine months ended September 30, 2018 was $1.0 million and $3.2 million, respectively.

(10) ACCRUED LIABILITIES

Accrued liabilities consisted of the following (in thousands):

	As of	
	September 30, 2019	December 31, 2018
Payroll and related liabilities	$ 3,031	$ 3,620
Other	4,429	4,750
Total accrued liabilities	$ 7,460	$ 8,370

(11) PRODUCT WARRANTIES

Our products carry defined warranties for defects in materials or workmanship which, according to their terms, generally obligate us to pay the costs of supplying and shipping replacement parts to customers and, in certain instances, pay for labor and other costs to service products. Outstanding product warranty periods range from thirty days to, in limited circumstances, the lifetime of certain product components. We record a liability at the time of sale for the estimated costs of fulfilling future warranty claims. If necessary, we adjust the liability for specific warranty-related matters when they become known and are reasonably estimable. Estimated warranty expense is included in cost of sales, based on historical warranty claim experience and available product quality data. Warranty expense is affected by the performance of new products, significant manufacturing or design defects not discovered until after the product is delivered to the customer, product failure rates, and higher or lower than expected repair costs. If warranty expense differs from previous estimates, or if circumstances change such that the assumptions inherent in previous estimates are no longer valid, the amount of product warranty obligations is adjusted accordingly.

Changes in our product warranty obligations were as follows (in thousands):

	Nine Months Ended September 30,	
	2019	2018
Balance, beginning of period	$ 5,575	$ 6,117
Accruals	3,721	2,772
Payments	(3,923)	(3,183)
Balance, end of period	$ 5,373	$ 5,706

(12) ACCUMULATED OTHER COMPREHENSIVE LOSS

The following tables set forth the changes in accumulated other comprehensive (loss) income, net of tax (in thousands) for the periods presented:

	Unrealized Gain (Loss) on Available-for-Sale Securities	Gain (Loss) on Derivative Securities	Foreign Currency Translation Adjustments	Accumulated Other Comprehensive Loss
Balance, June 30, 2019	$ —	$ —	$ (926)	$ (926)
Current period other comprehensive loss before reclassifications			(177)	(177)
Net other comprehensive loss income during period	—	—	(177)	(177)
Balance, September 30, 2019	$ —	$ —	$ (1,103)	$ (1,103)

	Unrealized Gain (Loss) on Available-for-Sale Securities		Gain (Loss) on Derivative Securities		Foreign Currency Translation Adjustments		Accumulated Other Comprehensive Loss	
Balance, January 1, 2019	$	(6)	$	223	$	(1,126)	$	(909)
Current period other comprehensive income (loss) before reclassifications		19		(128)		23		(86)
Amounts reclassified from accumulated other comprehensive loss		(13)		(95)		—		(108)
Net other comprehensive income (loss) during period		6		(223)		23		(194)
Balance, September 30, 2019	$	—	$	—	$	(1,103)	$	(1,103)

	Unrealized Gain (Loss) on Available-for-Sale Securities		Gain (Loss) on Derivative Securities		Foreign Currency Translation Adjustments		Accumulated Other Comprehensive (Loss) Income	
Balance, June 30, 2018	$	(67)	$	372	$	(866)	$	(561)
Current period other comprehensive income before reclassifications		40		28		82		150
Amounts reclassified from accumulated other comprehensive loss		—		(46)		—		(46)
Net other comprehensive income (loss) during period		40		(18)		82		104
Balance, September 30, 2018	$	(27)	$	354	$	(784)	$	(457)

	Unrealized Loss on Available-for-Sale Securities		Gain (Loss) on Derivative Securities		Foreign Currency Translation Adjustments		Accumulated Other Comprehensive Loss	
Balance, January 1, 2018	$	(64)	$	216	$	(411)	$	(259)
Current period other comprehensive income (loss) before reclassifications		37		242		(373)		(94)
Amounts reclassified from accumulated other comprehensive loss		—		(104)		—		(104)
Net other comprehensive income (loss) during period		37		138		(373)		(198)
Balance, September 30, 2018	$	(27)	$	354	$	(784)	$	(457)

(13) STOCK REPURCHASE PROGRAM

On February 21, 2018 our Board of Directors authorized a $15.0 million share repurchase program. Under this program, shares of our common stock may be repurchased from time to time through February 21, 2020. As of September 30, 2019, repurchases under this program totaled $1.0 million.

Repurchases may be made under the program in open market transactions at prevailing prices, in privately negotiated transactions, or by other means in accordance with federal securities laws. Share repurchases will be funded from existing cash balances, and repurchased shares will be retired and returned to unissued authorized shares.

As of September 30, 2019, there was $14.0 million remaining available for repurchases under the share repurchase program.

Cumulative repurchases pursuant to the program are as follows:

Quarter Ended	Number of Shares	Repurchased Amount	Average Price Per Share
December 31, 2018	75,813	$ 1,008,652	$ 13.30
March 31, 2019	—	—	—
June 30, 2019	—	—	—
September 30, 2019	—	—	—
Totals to date	75,813	$ 1,008,652	$ 13.30

(14) INCOME (LOSS) PER SHARE

Basic per share amounts were computed using the weighted average number of common shares outstanding. Diluted per share amounts were calculated using the number of basic weighted average shares outstanding increased by dilutive potential common shares related to stock-based awards, as determined by the treasury stock method. The weighted average numbers of shares outstanding used to compute income (loss) per share were as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Shares used to calculate basic income (loss) per share	29,728	30,185	29,660	30,230
Dilutive effect of outstanding stock options, performance stock units and restricted stock units	—	248	—	270
Shares used to calculate diluted income (loss) per share	29,728	30,433	29,660	30,500

The weighted average numbers of shares outstanding listed in the table below were anti-dilutive and excluded from the computation of diluted income per share. In the case of stock options, this is because the average market price did not exceed the exercise price.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Stock options	—	—	76	—
Restricted stock units	7	—	7	—

In the case of restricted stock units, this is because unrecognized compensation expense exceeds the current value of the awards (i.e., grant date market value was higher than current average market price). These shares may be dilutive potential common shares in the future (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Stock options	534	9	85	10
Restricted stock units	765	1	227	—

(15) SEGMENT AND ENTERPRISE-WIDE INFORMATION

We have two operating segments, Direct and Retail. There were no changes in our operating segments during the nine months ended September 30, 2019.

We evaluate performance using several factors, of which the primary financial measures are net sales and reportable segment contribution. Contribution is the measure of profit or loss, defined as net sales less product costs and directly attributable expenses. Directly attributable expenses include selling and marketing expenses, general and administrative expenses, and research and development expenses that are directly related to segment operations. Segment assets are those directly assigned to an operating segment's operations, primarily accounts receivable, inventories, goodwill and other intangible assets. Unallocated assets primarily include cash and cash equivalents, available-for-sale securities, derivative securities, shared information technology infrastructure, distribution centers, corporate headquarters, prepaids and other current assets, deferred income tax assets and other assets. Capital expenditures directly attributable to the Direct and Retail segments were not significant in any period.

Following is summary information by reportable segment (in thousands):

	Three Months Ended September 30, 2019	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2019	Nine Months Ended September 30, 2018
Net sales:				
Direct	$ 16,197	$ 28,955	$ 83,745	$ 134,980
Retail	44,823	61,490	119,097	143,668
Royalty	688	612	2,270	2,720
Consolidated net sales	$ 61,708	$ 91,057	$ 205,112	$ 281,368
Contribution:				
Direct	$ (8,693)	$ (1,363)	$ (19,569)	$ 10,667
Retail	4,772	12,707	3,803	20,196
Royalty	688	612	2,270	2,717
Consolidated contribution	$ (3,233)	$ 11,956	$ (13,496)	$ 33,580
Reconciliation of consolidated contribution to (loss) income from continuing operations:				
Consolidated contribution	$ (3,233)	$ 11,956	$ (13,496)	$ 33,580
Amounts not directly related to segments:				
Operating expenses	(5,020)	(5,796)	(90,338)	(15,521)
Other (expense) income, net	(422)	213	(910)	236
Income tax (expense) benefit	(1,900)	(1,870)	6,941	(4,645)
(Loss) income from continuing operations	$ (10,575)	$ 4,503	$ (97,803)	$ 13,650

There was no material change in the allocation of assets by segment during the nine months ended September 30, 2019, and, accordingly, assets by segment are not presented.

The following customers accounted for 10% or more of total net sales as follows:

	Three Months Ended September 30, 2019	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2019	Nine Months Ended September 30, 2018
Amazon.com	18.7%	18.8%	14.1%	11.8%
Dick's Sporting Goods	19.3%	19.6%	10.2%	13.5%

(16) BORROWINGS

Line of Credit

On March 29, 2019, we entered into a Credit Agreement with JPMorgan Chase Bank, N.A. (“Chase Bank”) that provides for a $40.0 million revolving line of credit. The term of the Credit Agreement expires on March 29, 2022 and is secured by substantially all of our assets.

The Credit Agreement contains customary covenants for financings of this type, including, among other terms and conditions, revolving availability subject to a calculated borrowing base, minimum cash reserves and minimum fixed charge cover ratio covenants, as well as limitations and conditions on our ability to (i) create, incur, assume or be liable for indebtedness; (ii) dispose of assets outside the ordinary course of business; (iii) acquire, merge or consolidate with or into another person or entity; (iv) create, incur or allow any lien on any of our property; (v) make investments; or (vi) pay dividends or make distributions, in each case subject to certain exceptions. In addition, the Credit Agreement provides for certain events of default such as nonpayment of principal and interest when due thereunder, breaches of representations and warranties, noncompliance with covenants, acts of insolvency and default on indebtedness held by third parties (subject to certain limitations and cure periods), as well as a subjective acceleration clause.

Based on management's forecast, we have concluded that it is probable that we will not comply with the minimum fixed charge coverage ratio covenant of the Credit Agreement at the December 31, 2019 measurement date. In the event we are unable to obtain a waiver or otherwise remedy this expected covenant violation, we will classify the line of credit as a current liability in our December 31, 2019 financial statements if the covenant violation occurs. Under the terms of the Credit Agreement, the fixed charge cover ratio, as of the last day of any fiscal quarter, may not be less than 1.10 to 1.00 when measured on any trailing four quarter basis beginning on December 31, 2019. While we anticipate receiving waivers or modifications of the existing debt covenants, we are also pursuing alternative sources of funding.

The interest rate applicable to each advance under the revolving line of credit is based on either Chase Bank's floating prime rate or adjusted LIBOR, plus an applicable margin. As of September 30, 2019, our borrowing rate for line of credit advances was 4.10%.

As of September 30, 2019, we had $20.6 million of outstanding borrowings under the line of credit resulting primarily from our term loan payoff. As of September 30, 2019, we were in compliance with the financial covenants of the Credit Agreement and $12.7 million was available for borrowing under the line of credit. Any outstanding balance is due and payable on March 29, 2022.

(17) INCOME TAXES

We account for income taxes based on the asset and liability method, whereby deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts and the tax basis of existing assets and liabilities. Evaluating the need for, and amount of, a valuation allowance for deferred tax assets often requires significant judgment and extensive analysis of all available evidence on a jurisdiction-by-jurisdiction basis. Such judgments require us to interpret existing tax law and other published guidance as applied to our circumstances. As part of this assessment, we consider both positive and negative evidence. The weight given to the potential effect of positive and negative evidence must be commensurate with the extent to which the strength of the evidence can be objectivity verified.

Each quarter, we re-evaluate the potential realization of our deferred tax assets and if any adjustments to valuation allowance is appropriate. During our re-assessment in the third quarter of 2019, the company determined that it was no longer more likely than not that the tax benefits from the existing U.S domestic deferred tax assets would be realized due to the substantial amount of the accounting losses realized in the recent quarters combined with the downward financial trend of the current period and forecasted losses. As part of our assessment in the third quarter, we heavily weighted the negative evidence of our anticipated cumulative losses in the near-term. Consequently, we recorded, in the third quarter of 2019, $3.9 million of valuation allowance to reduce certain net deferred tax assets to their anticipated realizable value.

Should it be determined in the future that it is more likely than not that any part of deferred income tax assets will be realized, an appropriate amount of valuation allowance would be released during the period in which such an assessment is made.

(18) COMMITMENTS AND CONTINGENCIES

Guarantees, Commitments and Off-Balance Sheet Arrangements
As of September 30, 2019, we had $0.9 million standby letters of credit.

We have long lead times for inventory purchases and, therefore, must secure factory capacity from our vendors in advance. As of September 30, 2019, we had approximately $47.0 million in noncancelable market-based purchase obligations, primarily for inventory purchases expected to be received within the next twelve months. Purchase obligations can vary from quarter-to-quarter and versus the same period in prior years due to a number of factors, including the amount of products that are shipped directly to Retail customer warehouses versus through Nautilus warehouses.

In the ordinary course of business, we enter into agreements that require us to indemnify counterparties against third-party claims. These may include: agreements with vendors and suppliers, under which we may indemnify them against claims arising from use of their products or services; agreements with customers, under which we may indemnify them against claims arising from their use or sale of our products; real estate and equipment leases, under which we may indemnify lessors against third-party claims relating to the use of their property; agreements with licensees or licensors, under which we may indemnify the licensee or licensor against claims arising from their use of our intellectual property or our use of their intellectual property; and agreements with parties to debt arrangements, under which we may indemnify them against claims relating to their participation in the transactions.

The nature and terms of these indemnification obligations vary from contract to contract, and generally a maximum obligation is not stated within the agreements. We hold insurance policies that mitigate potential losses arising from certain types of indemnification obligations. Management does not deem these obligations to be significant to our financial position, results of operations or cash flows, and therefore, no related liabilities were recorded as of September 30, 2019.

Legal Matters

From time to time, in the ordinary course of business, we may be involved in various claims, lawsuits and other proceedings. These legal and tax proceedings involve uncertainty as to the eventual outcomes and losses which may be realized when one or more future events occur or fail to occur.

We regularly monitor our estimated exposure to these contingencies and, as additional information becomes known, may change our estimates accordingly. We evaluate, on a quarterly basis, developments in legal proceedings, investigations or claims that could affect the amount of any accrual, as well as any developments that would make a loss probable or reasonably possible, and whether the amount of a probable or reasonably possible loss is estimable. Among other factors, we evaluate the advice of internal and external counsel, the outcomes from similar litigation, current status of the lawsuits (including settlement initiatives), legislative developments and other factors. Due to the numerous variables associated with these judgments and assumptions, both the precision and reliability of the resulting estimates of the related loss contingencies are subject to substantial uncertainties. Further, while we face contingencies that are reasonably possible to occur, we are unable to estimate the possible loss or range of loss at this time. As such, zero liability is recorded as of September 30, 2019.

As of the date of filing of this Quarterly Report on Form 10-Q, we were not involved in any material legal proceedings.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis is based upon our financial statements as of the dates and for the periods presented in this section. You should read this discussion and analysis in conjunction with the financial statements and notes thereto found in Part I, Item 1 of this Form 10-Q and our consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2018 (the "2018 Form 10-K"). All references to the third quarter and first nine months of 2019 and 2018 mean the three and nine-month periods ended September 30, 2019 and 2018, respectively. Unless the context otherwise requires, "Nautilus," "we," "us" and "our" refer to Nautilus, Inc. and its subsidiaries. Unless indicated otherwise, all information regarding our operating results pertains to our continuing operations.

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Words such as "plan," "expect," "aim," "believe," "project," "intend," "estimate," "will," "should," "could," and other terms of similar meaning typically identify forward-looking statements. Forward-looking statements include any statements related to our future business, financial performance or operating results; anticipated fluctuations in net sales due to seasonality; plans and expectations regarding gross and operating margins; plans and expectations regarding research and development expenses and capital expenditures and anticipated results from such expenditures and other investments in our capabilities and resources; anticipated losses from discontinued operations; plans for new product introductions, strategic partnerships and anticipated demand for our new and existing products; and statements regarding our inventory and working capital requirements and the sufficiency of our financial resources. These forward-looking statements, and others we make from time-to-time, are subject to a number of risks and uncertainties. Many factors could cause actual results to differ materially from those projected in forward-looking statements, including our ability to timely acquire inventory that meets our quality control standards from sole source foreign manufacturers at acceptable costs, changes in consumer fitness trends, changes in the media consumption habits of our target consumers or the effectiveness, availability and price of media time consistent with our cost and audience profile parameters, greater than anticipated costs or delays associated with launch of new products, weaker than expected demand for new or existing products, a decline in consumer spending due to unfavorable economic conditions, softness in the retail marketplace or the availability from retailers of heavily discounted competitive products, an adverse change in the availability of credit for our customers who finance their purchases, our ability to pass along vendor raw material price increases and other cost pressures, including increased shipping costs and unfavorable foreign currency exchange rates, our ability to hire and retain key management personnel, our ability to effectively develop, market and sell future products, our ability to protect our intellectual property, the introduction of competing products, and our ability to get foreign-sourced product through customs in a timely manner. Additional assumptions, risks and uncertainties are described in Part I, Item 1A, "Risk Factors," in our 2018 Form 10-K as supplemented or modified in our quarterly reports on Form 10-Q. We do not undertake any duty to update forward-looking statements after the date they are made or conform them to actual results or to changes in circumstances or expectations.

Overview

We are committed to providing innovative, quality solutions to help people achieve a fit and healthy lifestyle. Our principal business activities include designing, developing, sourcing and marketing high-quality cardio and strength fitness products and related accessories for consumer use, primarily in the U.S., Canada, Europe and Asia. Our products are sold under some of the most-recognized brand names in the fitness industry: Nautilus®, Bowflex®, Octane Fitness®, Schwinn® and Universal®.

We market our products through two distinct distribution channels, Direct and Retail, which we consider to be separate business segments. Our *Direct* business offers products directly to consumers through television advertising, the Internet and catalogs. Our *Retail* business offers our products through a network of independent retail companies and specialty retailers with stores and websites located in the U.S. and internationally. We also derive a portion of our revenue from the licensing of our brands and intellectual property.

Our results for the third quarter were primarily impacted by lower sales, however, we believe the appropriate improvements are being implemented into our overall business to address this trend. The primary actions taken include extensive, in-depth consumer insights research, which has identified an effective new positioning for the Bowflex brand, which is now underway through a new advertising campaign and updates to our website, television, social media, and other digital platforms. Additionally, we expect to launch many targeted new products across all our channels over the next few quarters. In parallel, we plan to continue our digital transformation with the inclusion of updated digital experience platforms on key new products, moving toward our goal of having all our products equipped with subscription-based digital experience offerings.

Net sales for the first nine months of 2019 were $205.1 million, reflecting a 27.1% decrease as compared to net sales of $281.4 million for the first nine months of 2018. Net sales of our Direct segment decreased by $51.2 million, or 38.0%, in the first nine months of 2019, compared to the first nine months of 2018, primarily driven by a reduction in advertising spending and lower sales of our Bowflex Max Trainer® product.

Net sales of our Retail segment decreased by $24.6 million, or 17.1%, in the first nine months of 2019, compared to the first nine months of 2018, primarily reflecting partial shipment delays due to recently imposed tariffs.

Royalty income for the first nine months of 2019 decreased by $0.5 million compared to the same period in the prior year, which included payment of royalties related to a new agreement.

Gross profit for the first nine months of 2019 was $72.4 million, or 35.3% of net sales, a decrease of $58.6 million, or 44.7%, as compared to gross profit of $131.0 million, or 46.6% of net sales, for the first nine months of 2018. The decrease in gross profit dollars was primarily due to lower sales coupled with lower gross margin percentages in both the Direct and Retail segments. Gross margin percentage points decreased by 11.3% in the first nine months of 2019 compared to the same period of the prior year primarily due to unfavorable product-mix and under absorption of operations fixed costs due to lower net sales.

Operating expenses for the first nine months of 2019 were $176.3 million, an increase of $63.3 million, or 56.0%, as compared to operating expenses of $113.0 million for the first nine months of 2018. The increase in operating expenses was primarily related to a goodwill and intangible impairment charge of $72.0 million partially offset by lower media spending and stock compensation expense.

Operating loss for the first nine months of 2019 was $103.8 million, a decrease of $121.9 million, or 675.0%, as compared to operating income of $18.1 million for the first nine months of 2018. The decrease in operating income for the first nine months of 2019 compared to the first nine months of 2018 was primarily driven by a goodwill and intangible impairment charge and lower gross margins associated with our sales during the period.

Loss from continuing operations was $97.8 million for the first nine months of 2019, or $3.30 per diluted share, compared to income from continuing operations of $13.7 million, or $0.45 per diluted share, for the first nine months of 2018. The effective tax rates for the first nine months of 2019 and 2018 were 6.6% and 25.4%, respectively. The 18.8% year-over-year percentage rate differential was due primarily to the goodwill impairment charge in the second quarter of 2019, for which no tax benefit was recognized, as well as the valuation allowance recorded in the third quarter of 2019, which together reduced the effective tax rate for the period.

Net loss for the first nine months of 2019 was $98.1 million, compared to net income of $13.3 million for the first nine months of 2018. Net loss per diluted share was $3.31 for the first nine months of 2019, compared to net income per diluted share of $0.44 for the first nine months of 2018.

Factors Affecting Our Performance

Our results of operations may vary significantly from period-to-period. Our revenues typically fluctuate due to the seasonality of our industry, customer buying patterns, product innovation, a digital transformation of health and fitness products, the nature and level of competition for health and fitness products, our ability to procure products to meet customer demand, the level of spending on, and effectiveness of, our media and advertising programs and our ability to attract new customers and maintain existing sales relationships. For example, sales are typically strongest in the fourth quarter due to holiday shopping and in the first quarter due to new year fitness goals. In addition, our revenues are highly susceptible to economic factors, including, among other things, the overall condition of the economy and the availability of consumer credit in both the U.S. and Canada. Our profit margins may vary in response to the aforementioned factors and our ability to manage product costs. Profit margins may also be affected by fluctuations in the costs or availability of materials used to manufacture our products, costs associated with acquisition or license of products and technologies, product warranty costs, the cost of fuel, foreign currency exchange rates, and changes in costs of other distribution or manufacturing-related services. Our operating profits or losses may also be affected by the efficiency and effectiveness of our organization, including executive management transition. Historically, our operating expenses have been influenced by media costs to produce and distribute advertisements of our products on television, the Internet and other media, facility costs, operating costs of our information and communications systems, product supply chain management, customer support and new product development activities and enhancements to existing products. In addition, our operating expenses have been affected from time-to-time by asset impairment charges, restructuring charges and other significant unusual or infrequent expenses.

As a result of the above and other factors, our period-to-period operating results may not be indicative of future performance. You should not place undue reliance on our operating results and should consider our prospects in light of the risks, expenses and difficulties typically encountered by us and other companies, both within and outside our industry. We may not be able to successfully address these risks and difficulties and, consequently, we cannot assure you of any future growth or profitability. For more information, see our discussion of risk factors located at Part I, Item 1A of our 2018 Form 10-K.

Discontinued Operations

Results from discontinued operations relate to the disposal of our former Commercial business, which was completed in April 2011. We reached substantial completion of asset liquidation at December 31, 2012. Although there was no revenue related to the Commercial business in either the 2019 or 2018 periods, we continue to incur product liability and other legal expenses associated with product previously sold into the Commercial channel.

RESULTS OF OPERATIONS

Results of operations information was as follows (dollars in thousands):

	Three Months Ended September 30,		Change	
	2019	2018	$	%
Net sales	$ 61,708	$ 91,057	$ (29,349)	(32.2)%
Cost of sales	42,641	52,551	(9,910)	(18.9)%
Gross profit	19,067	38,506	(19,439)	(50.5)%
Operating expenses:				
Selling and marketing	17,472	20,635	(3,163)	(15.3)%
General and administrative	6,726	7,503	(777)	(10.4)%
Research and development	3,122	4,208	(1,086)	(25.8)%
Total operating expenses	27,320	32,346	(5,026)	(15.5)%
Operating (loss) income	(8,253)	6,160	(14,413)	(234.0)%
Other (expense) income:				
Interest income	—	269	(269)	
Interest expense	(293)	(244)	(49)	
Other, net	(129)	188	(317)	
Total other (expense) income, net	(422)	213	(635)	
(Loss) income from continuing operations before income taxes	(8,675)	6,373	(15,048)	
Income tax expense	1,900	1,870	30	
(Loss) income from continuing operations	(10,575)	4,503	(15,078)	
Loss from discontinued operations, net of taxes	(114)	(194)	80	
Net (loss) income	$ (10,689)	$ 4,309	$ (14,998)	

	Nine Months Ended September 30,		Change	
	2019	2018	$	%
Net sales	$ 205,112	$ 281,368	$ (76,256)	(27.1)%
Cost of sales	132,686	150,343	(17,657)	(11.7)%
Gross profit	72,426	131,025	(58,599)	(44.7)%
Operating expenses:				
Selling and marketing	69,146	79,482	(10,336)	(13.0)%
General and administrative	23,824	20,740	3,084	14.9 %
Research and development	11,282	12,744	(1,462)	(11.5)%
Goodwill and intangible impairment charge	72,008	—	72,008	— %
Total operating expenses	176,260	112,966	63,294	56.0 %
Operating (loss) income	(103,834)	18,059	(121,893)	(675.0)%
Other (expense) income:				
Interest income	162	835	(673)	
Interest expense	(721)	(805)	84	
Other, net	(351)	206	(557)	
Total other (expense) income, net	(910)	236	(1,146)	
(Loss) income from continuing operations before income taxes	(104,744)	18,295	(123,039)	
Income tax (benefit) expense	(6,941)	4,645	(11,586)	
(Loss) income from continuing operations	(97,803)	13,650	(111,453)	
Loss from discontinued operations, net of taxes	(329)	(354)	25	
Net (loss) income	$ (98,132)	$ 13,296	$ (111,428)	

Results of operations information by segment was as follows (dollars in thousands):

	Three Months Ended September 30,		Change	
	2019	2018	$	%
Net sales:				
Direct	$ 16,197	$ 28,955	$ (12,758)	(44.1)%
Retail	44,823	61,490	(16,667)	(27.1)%
Royalty	688	612	76	12.4 %
	$ 61,708	$ 91,057	$ (29,349)	(32.2)%
Cost of sales:				
Direct	$ 9,987	$ 12,376	$ (2,389)	(19.3)%
Retail	32,654	40,175	(7,521)	(18.7)%
	$ 42,641	$ 52,551	$ (9,910)	(18.9)%
Gross profit:				
Direct	$ 6,210	$ 16,579	$ (10,369)	(62.5)%
Retail	12,169	21,315	(9,146)	(42.9)%
Royalty	688	612	76	12.4 %
	$ 19,067	$ 38,506	$ (19,439)	(50.5)%
Gross margin:				
Direct	38.3%	57.3%	(1,900)	basis points
Retail	27.1%	34.7%	(760)	basis points

	Nine Months Ended September 30,		Change	
	2019	2018	$	%
Net sales:				
Direct	$ 83,745	$ 134,980	$ (51,235)	(38.0)%
Retail	119,097	143,668	(24,571)	(17.1)%
Royalty	2,270	2,720	(450)	(16.5)%
	$ 205,112	$ 281,368	$ (76,256)	(27.1)%
Cost of sales:				
Direct	$ 42,112	$ 52,805	$ (10,693)	(20.2)%
Retail	90,574	97,535	(6,961)	(7.1)%
Royalty	—	3	(3)	(100.0)%
	$ 132,686	$ 150,343	$ (17,657)	(11.7)%
Gross profit:				
Direct	$ 41,633	$ 82,175	$ (40,542)	(49.3)%
Retail	28,523	46,133	(17,610)	(38.2)%
Royalty	2,270	2,717	(447)	(16.5)%
	$ 72,426	$ 131,025	$ (58,599)	(44.7)%
Gross margin:				
Direct	49.7%	60.9%	(1,120)	basis points
Retail	23.9%	32.1%	(820)	basis points

The following table compares the net sales of our major product lines within each business segment (dollars in thousands):

	Three Months Ended September 30,		Change	
	2019	2018	$	%
Direct net sales:				
Cardio products(1)	$ 12,431	$ 24,353	$ (11,922)	(49.0)%
Strength products(2)	3,766	4,602	(836)	(18.2)%
	16,197	28,955	(12,758)	(44.1)%
Retail net sales:				
Cardio products(1)	35,509	48,294	(12,785)	(26.5)%
Strength products(2)	9,314	13,196	(3,882)	(29.4)%
	44,823	61,490	(16,667)	(27.1)%
Royalty	688	612	76	12.4 %
	$ 61,708	$ 91,057	$ (29,349)	(32.2)%

	Nine Months Ended September 30,		Change	
	2019	2018	$	%
Direct net sales:				
Cardio products(1)	$ 68,121	$ 118,026	$ (49,905)	(42.3)%
Strength products(2)	15,624	16,954	(1,330)	(7.8)%
	83,745	134,980	(51,235)	(38.0)%
Retail net sales:				
Cardio products(1)	92,250	114,916	(22,666)	(19.7)%
Strength products(2)	26,847	28,752	(1,905)	(6.6)%
	119,097	143,668	(24,571)	(17.1)%
Royalty	2,270	2,720	(450)	(16.5)%
	$ 205,112	$ 281,368	$ (76,256)	(27.1)%

(1) Cardio products include: Max Trainer®, TreadClimber®, HVT™, LateralX®, Zero Runner®, treadmills, exercise bikes and ellipticals.

(2) Strength products include: home gyms, selectorized dumbbells, kettlebell weights and accessories.

Direct

Direct net sales decreased by 44.1% for the three month period ended September 30, 2019 compared to the same period of 2018, primarily reflecting a decline in sales of the Bowflex Max Trainer® products. Year-over-year sales were also lower due to reduced media spending of 37.0% in the three month period ended September 30, 2019 compared to the same period of 2018.

For the nine months ended September 30, 2019, Direct net sales decreased by 38.0% compared to the same period of 2018, primarily due to a 42.3% decline in cardio product sales, which was largely related to Bowflex Max Trainer® products and a reduction in advertising spending. Improvements are being implemented that we believe should be effective in addressing this trend. The primary actions taken include extensive, in-depth consumer insights research, which has identified an effective new positioning for the Bowflex brand, which is now underway through a new advertising campaign and updates to our website, television, social media and other digital platforms.

Combined consumer credit approvals by our primary and secondary U.S. third-party financing providers for the third quarter of 2019 were 51.0%, compared to 54.5% in the same period of 2018. The decrease in approvals reflects lower credit quality applications.

For the three and nine month periods ended September 30, 2019, cost of sales of our Direct business decreased by $2.4 million and $10.7 million, respectively, as compared to the same periods of 2018, due to the decreases in net sales.

For the three and nine month periods ended September 30, 2019, Direct gross margins decreased by 1,900 and 1,120 basis points, respectively, as compared to the same periods of 2018, primarily due to unfavorable overhead absorption related to decreased net sales and unfavorable product mix.

Retail

Retail net sales decreased by 27.1% and 17.1% for the three and nine month periods ended September 30, 2019, respectively, compared to the same periods of 2018. The decreases in the three and nine month periods were primarily due to partial shipment delays due to recently imposed tariffs until the beginning of the fourth quarter of 2019 and a decline in Bowflex Max Trainer® product sales in the segment. We expect sales in the last quarter of 2019 to include planned new product introductions and in-store merchandising with key customers.

The decreases in cost of sales of our Retail business for the three and nine month periods ended September 30, 2019 compared to the same periods of 2018 were primarily related to the decreases in net sales.

For the three and nine month periods ended September 30, 2019, Retail gross margins decreased by 760 and 820 basis points, respectively, compared to the same periods of 2018, due to unfavorable product mix and unfavorable overhead absorption related to decreased net sales.

Operating Expenses

Operating expenses for the first nine months of 2019 were $176.3 million, an increase of $63.3 million, or 56.0%, as compared to operating expenses of $113.0 million for the first nine months of 2018. The increase in operating expenses was primarily related to a goodwill and intangible impairment charge of $72.0 million, partially offset by lower media spending.

Selling and Marketing

Selling and marketing expenses include payroll, employee benefits, and other headcount-related expenses associated with sales and marketing personnel, and the costs of media advertising, promotions, trade shows, seminars, and other programs.

Dollars in thousands	Three Months Ended September 30,		Change	
	2019	2018	$	%
Selling and marketing	$17,472	$20,635	$(3,163)	(15.3)%
As % of net sales	28.3%	22.7%		

Dollars in thousands	Nine Months Ended September 30,		Change	
	2019	2018	$	%
Selling and marketing	$69,146	$79,482	$(10,336)	(13.0)%
As % of net sales	33.7%	28.2%		

The decreases in selling and marketing expense in the three and nine month periods ended September 30, 2019 compared to the same periods of 2018 were primarily due to lower media spending of $3.4 million and $10.5 million, respectively. The decreases in the three and nine month periods ended September 30, 2019 were partially offset by increased advertising production costs. We launched a major new multi-media advertising and communication campaign behind the Bowflex brand and new products during the third quarter of 2019.

Media advertising expense of our Direct business is the largest component of selling and marketing and was as follows:

Dollars in thousands	Three Months Ended September 30,		Change	
	2019	2018	$	%
Media advertising	$5,757	$9,142	$(3,385)	(37.0)%

Dollars in thousands	Nine Months Ended September 30,		Change	
	2019	2018	$	%
Media advertising	$32,012	$42,510	$(10,498)	(24.7)%

The decreases in media advertising for the three and nine months ended September 30, 2019 as compared to the same periods of 2018 reflected a reduction in spending resulting from unfavorable media return on investments.

General and Administrative

General and administrative expenses include payroll, employee benefits, stock-based compensation expense, and other headcount-related expenses associated with finance, legal, facilities, certain human resources and other administrative personnel, and other administrative fees.

Dollars in thousands	Three Months Ended September 30,		Change	
	2019	**2018**	**$**	**%**
General and administrative	$6,726	$7,503	$(777)	(10.4)%
As % of net sales	10.9%	8.2%		

Dollars in thousands	Nine Months Ended September 30,		Change	
	2019	**2018**	**$**	**%**
General and administrative	$23,824	$20,740	$3,084	14.9%
As % of net sales	11.6%	7.4%		

The decrease in general and administrative for the three month period ended September 30, 2019 compared to the same period of 2018 was primarily driven by lower litigation expense.

The increase in general and administrative for the nine months ended September 30, 2019 as compared to the same period of 2018 was primarily related to increases in litigation settlement expense and litigation expense of $2.0 million and $1.2 million, respectively.

Research and Development

Research and development expenses include payroll, employee benefits, other headcount-related expenses and information technology associated with product development.

Dollars in thousands	Three Months Ended September 30,		Change	
	2019	**2018**	**$**	**%**
Research and development	$3,122	$4,208	$(1,086)	(25.8)%
As % of net sales	5.1%	4.6%		

Dollars in thousands	Nine Months Ended September 30,		Change	
	2019	**2018**	**$**	**%**
Research and development	$11,282	$12,744	$(1,462)	(11.5)%
As % of net sales	5.5%	4.5%		

The decreases in research and development in the three and nine month periods ended September 30, 2019 as compared to the same periods of 2018 were primarily due to increases in capitalized internal labor and decreases in third-party application development expense.

Goodwill and Intangible Impairment Charge

In accordance ASC 350 — Intangibles — *Goodwill and Other*, we perform a goodwill and indefinite-lived asset impairment evaluation during the fourth quarter of each year. However, as a result of the decline in our market value relative to the market and our industry, identified as a triggering event, we performed an interim evaluation and a market capitalization reconciliation during the second quarter of 2019, which resulted in a non-cash goodwill and indefinite-lived intangible assets impairment charge of $72.0 million.

ASC 350 requires us to make significant assumptions and estimates about the extent and timing of future cash flows, discount rates, growth rates and terminal value. The cash flows are estimated over a significant future period of time, which makes those estimates and assumptions subject to an even higher degree of uncertainty. We also use market valuation models and other financial ratios, which require us to make certain assumptions and estimates regarding the applicability of those models to our assets and businesses.

In accordance ASC 360 — *Property, Plant, and Equipment* and other long-lived assets, we performed a test for recoverability of our assets as the goodwill and indefinite-lived intangible asset impairment created a triggering event. The long-lived assets were recoverable and no impairment was required.

For additional information related to our goodwill and intangible impairment charge, see Notes 4 and 8.

Operating (Loss) Income

Operating loss for the first nine months of 2019 was $103.8 million, a decrease of $121.9 million, or 675.0%, as compared to operating income of $18.1 million for the first nine months of 2018. The decrease in operating income for the first nine months of 2019 compared to the first nine months of 2018 was primarily driven by a goodwill and other intangible impairment charge and lower gross margins associated with our sales during the period.

Other, Net

Other, net relates to the effect of exchange rate fluctuations with the U.S. and our foreign subsidiaries.

Income Tax Expense

Income tax provision includes U.S. and international income taxes, and interest and penalties on uncertain tax positions.

Dollars in thousands	Three Months Ended September 30,		Change	
	2019	2018	$	%
Income tax expense	$1,900	$1,870	$30	1.6%
Effective tax rate	(21.9)%	29.3%		

Dollars in thousands	Nine Months Ended September 30,		Change	
	2019	2018	$	%
Income tax (benefit) expense	$(6,941)	$4,645	$(11,586)	*
Effective tax rate	6.6%	25.4%		

* Not meaningful.

Income tax provisions from continuing operations for the three and nine month periods ended September 30, 2019 were an expense of $1.9 million and a benefit of $6.9 million, respectively. Each quarter, we re-evaluate the potential realization of our deferred tax assets, considering both positive and negative evidence, including cumulative income or loss for the past three years and forecasted taxable income or loss. As a result of this re-evaluation during the third quarter of 2019, we concluded that $3.9 million of valuation allowance is required to reduce certain net deferred tax assets to their anticipated realizable value. The remaining value of the deferred tax assets was determined by evaluating the potential to recover the value of these assets through future reversal of certain existing deferred tax liabilities. The reduced effective tax rate from continuing operations for the nine month period ended September 30, 2019 was primarily due to the goodwill impairment in the second quarter of 2019, for which no tax benefit was recognized, combined with the valuation allowance recorded in the third quarter of 2019. Income tax expense from continuing operations for the three and nine month periods ended September 30, 2018 was primarily related to our income generated in the U.S.

See Note 17 of Notes to Condensed Consolidated Financial Statements for additional information.

LIQUIDITY AND CAPITAL RESOURCES

As of September 30, 2019, we had $5.8 million of cash and cash equivalents compared to $63.5 million of cash, cash equivalents and investments as of December 31, 2018. We expect our cash and cash equivalents and amounts available under our line of credit at September 30, 2019, along with cash expected to be generated from operations, to be sufficient to fund our operating and capital requirements for at least twelve months from September 30, 2019. Our future capital requirements may vary materially from those currently planned and will depend on many factors, including our levels of revenue, the timing and extent of spending on research and development efforts and other business initiatives, the expansion of sales and marketing activities, the timing of new product introductions, market acceptance of our products, and overall economic conditions. To the extent that current and anticipated future sources of liquidity are insufficient to fund our future business activities and requirements, we may be required to seek additional equity or debt financing. The sale of additional equity would result in additional dilution to our stockholders. The incurrence of debt financing would result in debt service obligations and the instruments governing such debt could provide for operating and financing covenants that would restrict our operations.

Cash used in operating activities was $35.6 million for the nine months ended September 30, 2019, compared to cash provided by operating activities of $9.8 million for the nine months ended September 30, 2018.

The decrease in cash flows from operating activities for the nine months ended September 30, 2019 as compared to the same period of 2018 was primarily due to the decrease in operating performance, along with the changes in our operating assets and liabilities discussed below.

Trade receivables decreased by $15.0 million to $30.9 million as of September 30, 2019, compared to $45.8 million as of December 31, 2018, primarily due to the seasonality of the business. Trade receivables as of September 30, 2019 compared to September 30, 2018 decreased by $15.3 million due to the lower Retail segment net sales in the third quarter of 2019.

Inventories decreased by $18.4 million to $50.1 million as of September 30, 2019, compared to $68.5 million as of December 31, 2018 primarily due to seasonality and our efforts to reduce the high level of ending inventory from the previous year. Inventories as of September 30, 2019 compared to September 30, 2018 decreased by $5.5 million, primarily due to our efforts to reduce inventory.

Prepaid and other current assets decreased by $1.8 million to $6.2 million as of September 30, 2019, compared to $8.0 million as of December 31, 2018, primarily due to lower prepaid marketing expenses. This was partially offset by increases to prepaid insurance and information technology expenses.

Trade payables decreased by $48.8 million to $38.5 million as of September 30, 2019, compared to $87.3 million as of December 31, 2018, primarily due to seasonality of the business and inventory related payments. Trade payables as of September 30, 2019, compared to September 30, 2018, decreased by $29.2 million primarily due to timing and overall reduction of inventory related payments.

Accrued liabilities decreased by $0.9 million to $7.5 million as of September 30, 2019, compared to $8.4 million as of December 31, 2018, primarily due to decreases in payroll and related liabilities and other accruals.

Cash provided by investing activities of $15.1 million for the first nine months of 2019 was primarily related to $25.3 million of net maturities of marketable securities, partially offset by $6.6 million of capital expenditures for implementation of new software systems, and production tooling and equipment and equity investments of $3.5 million. We anticipate spending between $8.0 million and $10.0 million in 2019 for digital platform enhancements, systems integration, and production tooling.

During the nine months ended September 30, 2019, we invested $3.5 million in non-controlling equity securities without readily determinable fair values. The carrying amount of the investment was recorded at cost and will be adjusted for any impairments and observable price changes under the election of the measurement alternative, with such changes recognized in earnings.

Cash used in financing activities of $11.3 million for the first nine months of 2019 was primarily related to loan principal repayments of $31.7 million, partially offset by proceeds from line of credit of $20.2 million.

Financing Arrangements

We have a Credit Agreement with JPMorgan Chase Bank, N.A. (“Chase Bank”) that provides for a $40.0 million revolving line of credit. The term of the Credit Agreement expires on March 29, 2022 and is secured by substantially all of our assets.

The Credit Agreement contains customary covenants for financings of this type, including, among other terms and conditions, revolving availability subject to a calculated borrowing base, minimum cash reserves and minimum fixed charge cover ratio covenants, as well as limitations and conditions on our ability to (i) create, incur, assume or be liable for indebtedness; (ii) dispose of assets outside the ordinary course of business; (iii) acquire, merge or consolidate with or into another person or entity; (iv) create, incur or allow any lien on any of our property; (v) make investments; or (vi) pay dividends or make distributions, in each case subject to certain exceptions. In addition, the Credit Agreement provides for certain events of default such as nonpayment of principal and interest when due thereunder, breaches of representations and warranties, noncompliance with covenants, acts of insolvency and default on indebtedness held by third parties (subject to certain limitations and cure periods), as well as a subjective acceleration clause.

Based on management's forecast, we have concluded that it is probable that we will not comply with the minimum fixed charge coverage ratio covenant of the Credit Agreement at the December 31, 2019 measurement date. In the event we are unable to obtain a waiver or otherwise remedy this expected covenant violation, we will classify the line of credit as a current liability in our December 31, 2019 financial statements if the covenant violation occurs. Under the terms of the Credit Agreement, the fixed charge cover ratio, as of the last day of any fiscal quarter, may not be less than 1.10 to 1.00 when measured on any trailing four quarter basis beginning on December 31, 2019. While we anticipate receiving waivers or modifications of the existing debt covenants, we are also pursuing alternative sources of funding.

The interest rate applicable to each advance under the revolving line of credit is based on either Chase Bank's floating prime rate or adjusted LIBOR, plus an applicable margin. As of September 30, 2019, our borrowing rate for line of credit advances was 4.10%.

As of September 30, 2019, we had $20.6 million of outstanding borrowings under the line of credit. As of September 30, 2019, we were in compliance with the financial covenants of the Credit Agreement and $12.7 million was available for borrowing under the line of credit.

During the three months ended March 31, 2019, we paid down our existing term loan of $32.0 million and refinanced the remaining portion with borrowings under our new line of credit.

Off-Balance Sheet Arrangements
In the ordinary course of business, we enter into agreements that require us to indemnify counterparties against third-party claims. These may include: agreements with vendors and suppliers, under which we may indemnify them against claims arising from our use of their products or services; agreements with customers, under which we may indemnify them against claims arising from their use or sale of our products; real estate and equipment leases, under which we may indemnify lessors against third-party claims relating to the use of their property; agreements with licensees or licensors, under which we may indemnify the licensee or licensor against claims arising from their use of our intellectual property or our use of their intellectual property; and agreements with parties to debt arrangements, under which we may indemnify them against claims relating to their participation in the transactions.

The nature and terms of these indemnifications vary from contract to contract, and generally a maximum obligation is not stated. We hold insurance policies that mitigate potential losses arising from certain types of indemnifications. Management does not deem these obligations to be significant to our financial position, results of operations or cash flows, and therefore, no liabilities were recorded at September 30, 2019.

Stock Repurchase Program
On February 21, 2018 our Board of Directors authorized a $15.0 million share repurchase program. Under this program, shares of our common stock may be repurchased from time to time through February 21, 2020. As of December 31, 2018 we had repurchased 75,813 shares under this program at a weighted average price of $13.30 per share for a total purchase price of $1.0 million.

For the nine months ended September 30, 2019 no shares were repurchased. As of September 30, 2019, $14.0 million remained available for future repurchases under the share repurchase program.

Repurchases under the program may be made in open market transactions at prevailing prices, in privately negotiated transactions, or by other means in accordance with federal securities laws. Share repurchases will be funded from existing cash balances, and repurchased shares will be retired and returned to unissued authorized shares.

SEASONALITY

We expect our revenues from fitness equipment products to vary seasonally. Sales are typically strongest in the first and fourth quarters, followed by the third quarter, and are generally weakest in the second quarter. We believe that consumers tend to be involved in outdoor activities during the spring and summer months, including outdoor exercise, which impacts sales of indoor fitness equipment. Fourth quarter could be lower than expected due our customers and retailers lowering their holiday spending. This seasonality can have a significant effect on our inventory levels, working capital needs and resource utilization.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Effective January 1, 2019, we adopted ASC 842, *Leases (Topic 842)*. For information on the adoption of Topic 842, see Notes 1 and 9 of Notes to Condensed Consolidated Financial Statements included in Part I, Item 1.

Other than the changes related to adoption of ASC 842, our critical accounting policies and estimates have not changed from those discussed in our 2018 Form 10-K.

NEW ACCOUNTING PRONOUNCEMENTS

See Notes 1 and 9 of Notes to Condensed Consolidated Financial Statements included in Part I, Item 1 for a discussion of new accounting pronouncements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Interest Rate and Foreign Exchange Risk

Our exposure to market risk from changes in interest rates relates primarily to our cash equivalents, marketable securities, derivative assets and variable-rate debt obligations. Our cash equivalents mature within three months or less from the date of purchase. Marketable securities with original maturities of greater than three months and remaining maturities of less than one year are classified as short-term investments. Investments with maturities beyond one year may be classified as short-term based on their highly liquid nature and because such marketable securities represent the investment of cash that is available for current operations. We have classified our marketable securities as available-for-sale and, therefore, we may choose to sell or hold them as changes in the market occur. Because of the short-term nature of the instruments in our portfolio, a decline in interest rates would reduce our interest income over time, and an increase in interest rates may negatively affect the market price or liquidity of certain securities within the portfolio.

Our negotiated credit facilities generally charge interest based on a benchmark rate such as LIBOR. Fluctuations in short-term interest rates may cause interest payments on term loan principal and drawn amounts on the revolving line to increase or decrease. As of September 30, 2019, the outstanding balances on our credit facilities totaled $20.6 million.

As of June 30, 2019, we terminated a $20.0 million receive-variable, pay-fixed interest rate swap outstanding with Chase Bank and discontinued the cash flow hedge on our variable-rate term loan.

We enter into foreign exchange forward contracts to offset the earnings impacts of exchange rate fluctuations on certain monetary assets and liabilities. Total notional amounts outstanding at September 30, 2019 were $17.6 million.

A hypothetical 10% increase in interest rates, or a 10% movement in the currencies underlying our foreign currency derivative positions, would not have material impacts on our results of operations, financial position or cash flows. We do not enter into derivative instruments for any purpose other than to manage our interest rate or foreign currency exposure. That is, we do not engage in interest rate or currency exchange rate speculation using derivative instruments.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

In accordance with Rule 13a-15 of the Securities Exchange Act of 1934 (the “Exchange Act”), as of the end of the period covered by this Quarterly Report on Form 10-Q, our management evaluated, with the participation of our Principal Executive Officer and our Principal Financial and Accounting Officer, the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) and Rule 15d-15(e) under the Exchange Act). Based upon their evaluation of these disclosure controls and procedures, our management, including the Principal Executive Officer and Principal Financial and Accounting Officer, have concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the three months ended September 30, 2019, 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

From time to time, in the ordinary course of business, we may be involved in various claims, lawsuits and other proceedings. These legal and tax proceedings involve uncertainty as to the eventual outcomes and losses which may be realized when one or more future events occur or fail to occur.

As of the date of filing of this Quarterly Report on Form 10-Q, we were not involved in any material legal proceedings.

Item 1A. Risk Factors

We operate in an environment that involves a number of risks and uncertainties. The risks described below update the risk fators in Part I, Item 1A. Risk Factors in our 2018 Form 10-K. The risks and uncertainties described below and in our 2018 Form 10-K are not the only risks and uncertainties that we face. Additional risks and uncertainties that presently are not considered material or are not known to us, and therefore are not mentioned herein, may impair our business operations. If any of the risks described below or in our 2018 Form 10-K actually occur, our business, operating results and financial position could be adversely affected.

We have incurred indebtedness under the Credit Agreement, and if we fail to comply with the covenants and other obligations under the Credit Agreement, Chase Bank may accelerate amounts owed and may foreclose upon the assets securing our obligation.

On March 29, 2019, we entered into a Credit Agreement with Chase Bank that provides for a $40 million revolving line of credit. As of September 30, 2019, we had $20.6 million of outstanding borrowings under the line of credit which we used to pay off a term loan. As of September 30, 2019, we were in compliance with the financial covenants of the Credit Agreement and $12.7 million was available for borrowing under the line of credit.

The Credit Agreement matures on March 29, 2022. If we do not have sufficient funds to repay our debt when due, it may be necessary to refinance our debt through additional debt or equity financings. If, at the time of any refinancing, prevailing interest rates or other factors result in higher interest rates on such refinancing, increases in interest expense could have a material adverse effect on our business, results of operations and financial condition.

The Credit Agreement contains various affirmative and negative covenants that may restrict our ability to, among other things, permit liens on our property, change the nature of our business, transact business with affiliates, merge or consolidate with any other person or sell or convey certain of our assets. We currently anticipate that we will be in breach of the minimum fixed charge coverage ratio covenant as of December 31, 2019. Violation of this or any other covenant under the Credit Agreement could result in an event of default. If we are unable to cure or receive a waiver for a breach of the minimum fixed charge coverage ratio covenant or any other covenant under the Credit Agreement, we will be required to seek additional equity or debt financing, which we may not be able to obtain on favorable terms, if at all. If we need additional capital and cannot raise it on acceptable terms, our business, financial condition and operating results could be materially and adversely affected.

Upon the occurrence of an event of default that is not cured or waived, Chase Bank would have the ability to accelerate the repayment of all amounts then outstanding under the Credit Agreement and may foreclose on the assets securing our obligation. Any declaration of an event of default by Chase Bank would have a material adverse effect on our operating results, financial position and cash flows.

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Item 6. Exhibits

The following exhibits are filed herewith and this list is intended to constitute the exhibit index:

Exhibit No.	Description
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
31.2	Certification of Corporate Controller pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
32.1	Certification of Chief Executive Officer and Corporate Controller pursuant to Rule 13a-14(b) of the Securities and Exchange Act of 1934, as amended, and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

* Indicates management contract, compensatory agreement or arrangement, in which our directors or executive officers may participate.

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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.

NAUTILUS, INC.
(Registrant)

November 8, 2019	By:	/s/ **James Barr IV**
Date		James Barr IV Chief Executive Officer

NAUTILUS, INC.
(Registrant)

November 8, 2019	By:	/s/ **Sarah A. Jones**
Date		Sarah A. Jones Principal Financial and Accounting Officer

Exhibit 31.1

CERTIFICATION

I, James Barr IV, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Nautilus, 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.

November 8, 2019	By:	**/s/ James Barr IV**
Date		James Barr IV
		Chief Executive Officer

Exhibit 31.2

CERTIFICATION

I, Sarah A. Jones, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Nautilus, 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.

November 8, 2019	By:	**/s/ Sarah A. Jones**
Date		Sarah A. Jones
		Principal Financial and Accounting Officer

<u>**Exhibit 32.1**</u>

Certification
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
(Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code)

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), the undersigned officers of Nautilus, Inc., a Washington corporation (the “Company”), do hereby certify that:

To our knowledge, the Quarterly Report on Form 10-Q for the period ended September 30, 2019 (the “Form 10-Q”) of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

November 8, 2019	By:	**/s/ James Barr IV**
Date		James Barr IV
		Chief Executive Officer
November 8, 2019	By:	**/s/ Sarah A. Jones**
Date		Sarah A. Jones
		Principal Financial and Accounting Officer