

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended: July 7, 2001

OR

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

Commission file number: **0-19848**

FOSSIL, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

75-2018505

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

2280 N. Greenville, Richardson, Texas 75082

(Address of principal executive offices)
(Zip Code)

(972) 234-2525

(Registrant's telephone number, including area code)

Indicate by check mark whether registrant (1) has filed all reports to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

The number of shares of Registrant's common stock, outstanding as of August 17, 2001: 30,162,470.

PART 1 - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

FOSSIL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share amounts)

	July 7, 2001 (Unaudited)	December 30, 2000
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 67,252	\$ 79,501
Short-term marketable investments	5,328	11,312
Accounts receivable – net	56,003	62,876
Inventories	97,930	81,118
Deferred income tax benefits	7,500	7,779
Prepaid expenses and other current assets	<u>10,192</u>	<u>10,245</u>
Total current assets	244,205	252,831
Investment in joint venture	5,896	5,935
Property, plant and equipment – net	51,429	42,252
Intangible and other assets – net	<u>10,601</u>	<u>6,573</u>
	<u>\$ 312,131</u>	<u>\$ 307,591</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Notes payable	\$ 4,651	\$ 5,107
Accounts payable	14,933	18,325
Accrued expenses:		
Co-op advertising	10,947	14,320
Compensation	5,285	6,179
Other	18,981	19,145
Income taxes payable	<u>20,238</u>	<u>19,964</u>
Total current liabilities	75,035	83,040
Minority interest in subsidiaries	2,933	3,852
Stockholders' equity:		
Common stock, 30,162,791 and 30,136,824 shares issued and outstanding, respectively	301	301
Additional paid-in capital	13,730	14,214
Retained earnings	225,712	208,429
Accumulated other comprehensive loss	<u>(5,580)</u>	<u>(2,245)</u>
Total stockholders' equity	<u>234,163</u>	<u>220,699</u>
	<u>\$ 312,131</u>	<u>\$ 307,591</u>

See notes to condensed consolidated financial statements.

FOSSIL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
AND COMPREHENSIVE INCOME

UNAUDITED

(In thousands, except per share amounts)

	For the 13 Weeks Ended July 7, <u>2001</u>	For the 13 Weeks Ended July 1, <u>2000</u>	For the 27 Weeks Ended July 7, <u>2001</u>	For the 26 Weeks Ended July 1, <u>2000</u>
Net sales	\$ 112,357	\$ 113,393	\$ 233,462	\$ 216,962
Cost of sales	<u>55,453</u>	<u>56,833</u>	<u>116,823</u>	<u>106,743</u>
Gross profit	56,904	56,560	116,639	110,219
Operating expenses:				
Selling and distribution	34,545	27,329	67,127	51,512
General and administrative	<u>10,775</u>	<u>8,779</u>	<u>21,587</u>	<u>17,096</u>
Total operating expenses	<u>45,320</u>	<u>36,108</u>	<u>88,714</u>	<u>68,608</u>
Operating income	11,584	20,452	27,925	41,611
Interest expense	27	18	51	45
Other income (expense) – net	<u>588</u>	<u>(185)</u>	<u>932</u>	<u>88</u>
Income before income taxes	12,145	20,249	28,806	41,654
Provision for income taxes	<u>4,862</u>	<u>8,301</u>	<u>11,523</u>	<u>17,078</u>
Net income	\$ 7,283	\$ 11,948	\$ 17,283	\$ 24,576
Other comprehensive income, net of taxes:				
Currency translation adjustment	(2,603)	841	(4,123)	(1,188)
Unrealized (loss) gain on short-term investments	(5)	(33)	76	44
Forward contracts as hedge of intercompany foreign currency payments:				
Cumulative effect of implementing SFAS No. 133	-	-	(400)	-
Change in fair values	<u>431</u>	<u>-</u>	<u>1,112</u>	<u>-</u>
Total comprehensive income	<u>\$ 5,106</u>	<u>\$ 12,756</u>	<u>\$ 13,948</u>	<u>\$ 23,432</u>
Earnings per share:				
Basic	<u>\$ 0.24</u>	<u>\$ 0.37</u>	<u>\$ 0.57</u>	<u>\$ 0.77</u>
Diluted	<u>\$ 0.23</u>	<u>\$ 0.36</u>	<u>\$ 0.55</u>	<u>\$ 0.74</u>
Weighted average common shares outstanding:				
Basic	<u>30,073</u>	<u>32,107</u>	<u>30,125</u>	<u>32,108</u>
Diluted	<u>31,259</u>	<u>33,236</u>	<u>31,221</u>	<u>33,255</u>

See notes to condensed consolidated financial statements.

FOSSIL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
UNAUDITED
(In thousands)

	For the 27 Weeks Ended July 7, <u>2001</u>	For the 26 Weeks Ended July 1, <u>2000</u>
Operating activities:		
Net income	\$ 17,283	\$ 24,576
Noncash items affecting net income:		
Minority interest in subsidiaries	658	1,028
Equity in losses of joint ventures	204	385
Depreciation and amortization	4,258	2,936
Increase in allowance for doubtful accounts	251	468
Decrease in allowance for returns - net of related inventory in transit	(1,058)	(533)
Deferred income tax benefits	279	(364)
Changes in operating assets and liabilities:		
Accounts receivable	10,604	70
Inventories	(16,574)	(32,840)
Prepaid expenses and other current assets	56	(2,699)
Accounts payable	(7,891)	11,192
Accrued expenses	(5,465)	(9,592)
Income taxes payable	<u>983</u>	<u>1,005</u>
Net cash from (used in) operating activities	3,588	(4,368)
Investing activities:		
Additions to property, plant and equipment	(13,207)	(7,006)
Sale of marketable investments	5,984	6,080
Net assets acquired in business combinations	(5,121)	-
Investment in joint venture	(165)	(2,000)
Increase in intangible and other assets	<u>(244)</u>	<u>(321)</u>
Net cash used in investing activities	(12,753)	(3,247)
Financing activities:		
Issuance of common or treasury stock for stock option exercises	1,671	498
Acquisition and retirement of common stock	(3,539)	-
Purchase of treasury stock	-	(267)
Distribution of minority interest earnings	(676)	(493)
Repayments of notes payable-banks	<u>(456)</u>	<u>(185)</u>
Net cash used in financing activities	(3,000)	(447)
Effect of exchange rate changes on cash and cash equivalents	<u>(84)</u>	<u>(997)</u>
Net decrease in cash and cash equivalents	(12,249)	(9,059)
Cash and cash equivalents:		
Beginning of period	<u>79,501</u>	<u>90,908</u>
End of period	<u>\$ 67,252</u>	<u>\$ 81,849</u>

See notes to condensed consolidated financial statements.

FOSSIL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
UNAUDITED

1. FINANCIAL STATEMENT POLICIES

Basis of Presentation. The condensed consolidated financial statements include the accounts of Fossil, Inc., a Delaware corporation, and its majority-owned subsidiaries (the “Company”). The condensed consolidated financial statements reflect all adjustments that are, in the opinion of management, necessary to present a fair statement of the Company’s financial position as of July 7, 2001, and the results of operations for the thirteen-week periods ended July 7, 2001 and July 1, 2000, respectively and the twenty-seven week and twenty-six week periods ended July 7, 2001 and July 1, 2000, respectively. All adjustments are of a normal, recurring nature.

These interim financial statements should be read in conjunction with the audited financial statements and the notes thereto included in Form 10-K filed by the Company pursuant to the Securities Exchange Act of 1934 for the year ended December 30, 2000. Operating results for the thirteen and twenty-seven week periods ended July 7, 2001 are not necessarily indicative of the results to be achieved for the full year.

Business. The Company designs, develops, markets and distributes fashion watches and other accessories, principally under the “FOSSIL” and “RELIC” brands names. The Company’s products are sold primarily through department stores and other major retailers, both domestically and in over 80 countries worldwide.

2. INVENTORIES

Inventories consist of the following:

<i>(In thousands)</i>	July 7, <u>2001</u>	December 30, <u>2000</u>
Components and parts	\$ 5,460	\$ 6,258
Work-in-process	3,139	1,182
Finished merchandise on hand	65,193	48,113
Merchandise at Company stores	13,363	13,296
Merchandise in-transit from estimated customer returns	<u>10,775</u>	<u>12,269</u>
	<u>\$97,930</u>	<u>\$81,118</u>

3. FOREIGN CURRENCY HEDGING INSTRUMENTS

The Company periodically enters into forward contracts principally to hedge the future payment of intercompany inventory transactions with its non-U.S. subsidiaries. At July 7, 2001, the Company had hedge contracts to sell 18.4 million Euro for approximately \$17.0 million, expiring through December 2001. If the Company were to settle its Euro based contracts at that date, the net result would be a gain of approximately \$712,000, net of taxes for the twenty-seven week period ended July 7, 2001. This net unrealized gain is recognized in accounts payable and other comprehensive income under SFAS No. 133, “Accounting for Derivative Instruments and Hedging Activities.”

4. GEOGRAPHIC INFORMATION

(In thousands)

	For the 13 Weeks Ended		For the 13 Weeks Ended	
	July 7, 2001		July 1, 2000	
	<u>Net Sales</u>	<u>Operating Income</u>	<u>Net Sales</u>	<u>Operating Income</u>
U.S.- exclusive of Stores:				
External customers	\$ 58,965	\$ 6,292	\$ 62,813	\$ 8,890
Intergeographic	14,275	-	13,317	-
Far East and Export:				
External customers	11,255	7,215	16,354	9,361
Intergeographic	49,162	-	54,787	-
Stores	14,307	(2,373)	11,199	1,961
Europe	26,805	814	21,257	(17)
Japan	1,025	(364)	1,763	257
Intergeographic items	<u>(63,437)</u>	<u>-</u>	<u>(68,097)</u>	<u>-</u>
Consolidated	<u>\$112,357</u>	<u>\$11,584</u>	<u>\$113,393</u>	<u>\$20,452</u>

	For the 27 Weeks Ended		For the 26 Weeks Ended	
	July 7, 2001		July 1, 2000	
	<u>Net Sales</u>	<u>Operating Income</u>	<u>Net Sales</u>	<u>Operating Income</u>
U.S.- exclusive of Stores:				
External customers	\$127,290	\$ 19,233	\$128,010	\$ 19,299
Intergeographic	34,630	-	30,417	-
Far East and Export:				
External customers	24,036	14,010	24,572	17,393
Intergeographic	93,627	-	97,487	-
Stores	25,096	(5,544)	18,243	1,151
Europe	54,472	661	42,929	4,025
Japan	2,568	(435)	3,208	(257)
Intergeographic items	<u>(128,257)</u>	<u>-</u>	<u>(127,904)</u>	<u>-</u>
Consolidated	<u>\$233,462</u>	<u>\$27,925</u>	<u>\$216,962</u>	<u>\$41,611</u>

5. EARNINGS PER SHARE

The following table reconciles the numerators and denominators used in the computations of both basic and diluted EPS:

<i>(In thousands, except per share data)</i>	For the 13 Weeks Ended July 7, 2001	For the 13 Weeks Ended July 1, 2000	For the 27 Weeks Ended July 7, 2001	For the 26 Weeks Ended July 1, 2000
Basic EPS computation:				
Numerator:				
Net income	\$ <u>7,283</u>	\$ <u>11,948</u>	\$ <u>17,283</u>	\$ <u>24,576</u>
Denominator:				
Weighted average common shares outstanding	<u>30,073</u>	<u>32,107</u>	<u>30,125</u>	<u>32,108</u>
Basic EPS	\$ <u>0.24</u>	\$ <u>0.37</u>	\$ <u>0.57</u>	\$ <u>0.77</u>
Diluted EPS computation:				
Numerator:				
Net income	\$ <u>7,283</u>	\$ <u>11,948</u>	\$ <u>17,283</u>	\$ <u>24,576</u>
Denominator:				
Weighted average common shares outstanding	30,073	32,107	30,125	32,108
Stock option conversion	<u>1,186</u>	<u>1,129</u>	<u>1,096</u>	<u>1,147</u>
	<u>31,259</u>	<u>33,236</u>	<u>31,221</u>	<u>33,255</u>
Diluted EPS	\$ <u>0.23</u>	\$ <u>0.36</u>	\$ <u>0.55</u>	\$ <u>0.74</u>

6. ACQUISITIONS/JOINT VENTURES

On July 3, Fossil (East) Limited ("Fossil East") increased its equity interest in Pulse Time, Ltd. to 90% by acquiring an additional 30% of the capital stock from its minority holders in exchange for approximately 24,000 shares of the Company's common stock valued at \$450,000. Additionally, on July 3, 2001, Fossil East increased its equity interest in Trylink, Ltd. to 85% by acquiring an additional 34% of the capital stock from its minority holders in exchange for \$225,000 in cash and approximately 14,000 shares of the Company's common stock valued at \$225,000. Both these acquisitions have been accounted for as a purchase and no goodwill was recorded in connection with either transaction.

On July 9, 2001, the Company sold 50% of the equity of its wholly-owned subsidiary in Japan to Seiko Instruments Incorporated (SII) pursuant to a joint venture agreement for the marketing, distribution and sale of the Company's products in Japan. The Company accounted for this investment based upon the equity method from the effective date of the transaction. The Company does not expect this change in accounting to materially affect the results of operations for the remainder of its fiscal year.

On July 9, 2001, the Company acquired 80% of the capital stock of FSLA, Pty. Limited, the Company's current distributor in Australia, for a purchase price of approximately \$300,000. This acquisition will be recorded as a purchase and, in connection therewith, the Company will record goodwill of approximately \$200,000.

In August 2001, the Company acquired 99.6% of the outstanding capital stock of Vedette Industries, SA, the Company's current distributor in France, for a purchase price of approximately \$5.3 million paid in cash. The terms of this transaction include a future earnout payment of an amount up to \$1.5 million in the event that sales and operating income objectives are achieved. The acquisition will be recorded as a purchase and, in connection therewith, the Company will record goodwill of approximately \$1.0 million, including amounts relating to the earnout provision.

The results of these business combinations are included in the accompanying consolidated financial statements since the dates of their acquisition. The proforma effects, as if transactions had occurred at the beginning of the years presented, are not significant.

7. RECENT ACCOUNTING PRONOUNCEMENTS

In July 2001, the Financial Accounting Standards Board issued Statement No. 141 (SFAS No. 141), "Business Combinations," and Statement No. 142 (SFAS No. 142), "Goodwill and Other Intangible Assets." SFAS 142 includes requirements to test goodwill and indefinite lived intangible assets for impairment rather than amortize them. These standards will be adopted in fiscal 2002. The Company is currently evaluating the impact that these standards will have on its financial statements.

FOSSIL, INC. AND SUBSIDIARIES

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

The following is a discussion of the financial condition and results of operations of Fossil, Inc. and its majority owned subsidiaries (the "Company") for the thirteen and twenty-seven week periods ended July 7, 2001 (the "Second Quarter" and "Year To Date Period," respectively), as compared to the thirteen and twenty-six week periods ended July 1, 2000 (the "Prior Year Quarter" and "Prior Year YTD Period," respectively). This discussion should be read in conjunction with the Condensed Consolidated Financial Statements and the related Notes attached hereto.

General

The Company is a leader in the design, development, marketing and distribution of contemporary, high quality fashion watches and accessories. The FOSSIL brand name was developed by the Company to convey a distinctive fashion, quality and value message and a brand image reminiscent of "America in the 1950s" that suggests a time of fun, fashion and humor. Since its inception in 1984, the Company has grown from its original flagship FOSSIL watch product into a company offering a diversified range of accessories and apparel. The Company's current product offerings include an extensive line of fashion watches sold under the FOSSIL and RELIC brands, complementary lines of small leather goods, belts, handbags, sunglasses, jewelry and FOSSIL brand apparel. In addition to developing its own brands, the Company leverages its development and production expertise by designing and manufacturing private label and licensed products for some of the most prestigious companies in the world, including national retailers, entertainment companies and fashion designers.

The Company's products are sold primarily to department stores and specialty retail stores in over 80 countries worldwide through Company-owned foreign sales subsidiaries and through a network of 47 independent distributors. The Company's foreign operations include a presence in Asia, Australia, Canada, the Caribbean, Europe, Central and South America and the Middle East. In addition, the Company's products are offered at Company-owned retail locations throughout the United States and in independently-owned, authorized FOSSIL retail stores and kiosks located in several major airports, on cruise ships and in certain international markets. The Company's successful expansion of its product lines worldwide and leveraging of its infrastructure have contributed to its increasing net sales and operating profits during the last five fiscal years.

Second Quarter and Year To Date Period Highlights

- Despite a strong U.S. dollar, sales from the Company's European operations increased 26% and 27% during the Second Quarter and Year To Date Period, respectively.
- Sales from the Company's licensed watch line surpassed \$40 million during the Year To Date Period, a 34% increase over the Prior Year YTD Period.
- Leather product sales increased by 24% over the Prior Year YTD Period as FOSSIL handbags and RELIC brand leather lines continued to gain market share.
- Excluding the impact of an \$8.3 million non-branded premium watch sale in the prior year, which did not reoccur, other international sales which consist of export sales and sales from the Company's Far East operations increased 27% and 37% during the Second Quarter and Year To Date Period, respectively.
- The Company operated 78 retail locations consisting of 43 outlet, 18 accessory and 17 jeanswear stores at the end of the Second Quarter compared to 52 stores (35 outlet and 17 accessory) at the end of the Prior Year Quarter. This retail store expansion generated sales volume growth in excess of 37% for the Year To Date Period.

- The Company acquired The Avia Watch Company, increasing its sales and marketing presence in the U.K. and providing opportunities for the Company to leverage its existing infrastructure in this market.
- The Company acquired additional equity interests in two of its majority-owned factories in the Far East.

Results of Operations

The following table sets forth, for the periods indicated, (i) the percentages of the Company's net sales represented by certain line items from the Company's condensed consolidated statements of income and (ii) the percentage changes in these line items between the current periods and the comparable periods of the prior year.

	<u>Percentage of Net Sales</u>		<u>Percentage Change</u>	<u>Percentage of Net Sales</u>		<u>Percentage Change</u>
	<u>For the 13 Weeks Ended</u>		<u>For the 13 Weeks Ended</u>	<u>For the 27 Weeks Ended</u>	<u>For the 26 Weeks Ended</u>	<u>For the 27 Weeks Ended</u>
	<u>July 7, 2001</u>	<u>July 1, 2000</u>	<u>July 7, 2001</u>	<u>July 7, 2001</u>	<u>July 1, 2000</u>	<u>July 7, 2001</u>
Net sales	100.0%	100.0%	(0.9)%	100.0%	100.0%	7.6%
Cost of sales	<u>49.4</u>	<u>50.1</u>	(2.4)	<u>50.0</u>	<u>49.2</u>	9.4
Gross profit	50.6	49.9	0.6	50.0	50.8	5.8
Selling and distribution expenses	30.7	24.1	26.4	28.8	23.7	30.3
General and administrative expenses	<u>9.6</u>	<u>7.7</u>	22.7	<u>9.2</u>	<u>7.9</u>	26.3
Operating income	10.3	18.1	(43.4)	12.0	19.2	(32.9)
Interest expense	0.0	0.0	48.4	0.0	0.0	13.1
Other income (expense)- net	<u>0.5</u>	<u>(0.2)</u>	(418.6)	<u>0.3</u>	<u>0.0</u>	953.8
Income before income taxes	10.8	17.9	(40.0)	12.3	19.2	(30.8)
Income taxes	<u>4.3</u>	<u>7.4</u>	(41.4)	<u>4.9</u>	<u>7.9</u>	(32.5)
Net income	<u>6.5%</u>	<u>10.5%</u>	(39.0)%	<u>7.4%</u>	<u>11.3%</u>	(29.7)%

Net Sales. The following table sets forth certain components of the Company's consolidated net sales and the percentage relationship of the components to consolidated net sales for the periods indicated (in millions, except percentage data):

	<u>Amounts</u>		<u>% of Total</u>	
	<u>For the 13 Weeks Ended</u>		<u>For the 13 Weeks Ended</u>	
	<u>July 7, 2001</u>	<u>July 1, 2000</u>	<u>July 7, 2001</u>	<u>July 1, 2000</u>
International:				
Europe	\$ 26.8	\$ 21.2	24 %	19 %
Other	<u>12.3</u>	<u>18.1</u>	<u>11</u>	<u>16</u>
Total International	<u>39.1</u>	<u>39.3</u>	<u>35</u>	<u>35</u>
Domestic:				
Watch products	37.4	43.6	33	38
Other products	<u>21.6</u>	<u>19.2</u>	<u>19</u>	<u>17</u>
Total	59.0	62.8	52	55
Stores	<u>14.3</u>	<u>11.3</u>	<u>13</u>	<u>10</u>
Total Domestic	<u>73.3</u>	<u>74.1</u>	<u>65</u>	<u>65</u>
Total Net Sales	<u>\$112.4</u>	<u>\$113.4</u>	<u>100</u> %	<u>100</u> %

	<u>Amounts</u>		<u>% of Total</u>	
	<u>For the 27 Weeks Ended</u>	<u>For the 26 Weeks Ended</u>	<u>For the 27 Weeks Ended</u>	<u>For the 26 Weeks Ended</u>
	<u>July 7, 2001</u>	<u>July 1, 2000</u>	<u>July 7, 2001</u>	<u>July 1, 2000</u>
International:				
Europe	\$ 54.5	\$ 42.9	23 %	20 %
Other	<u>26.6</u>	<u>27.8</u>	<u>12</u>	<u>13</u>
Total International	<u>81.1</u>	<u>70.7</u>	<u>35</u>	<u>33</u>
Domestic:				
Watch products	76.3	85.0	32	39
Other products	<u>51.0</u>	<u>43.0</u>	<u>22</u>	<u>20</u>
Total	127.3	128.0	54	59
Stores	<u>25.1</u>	<u>18.3</u>	<u>11</u>	<u>8</u>
Total Domestic	<u>152.4</u>	<u>146.3</u>	<u>65</u>	<u>67</u>
Total Net Sales	<u>\$233.5</u>	<u>\$217.0</u>	<u>100</u> %	<u>100</u> %

The Company's net sales increased 9% during the Second Quarter, excluding the \$8.3 million non-branded premium watch sale in the Prior Year Quarter and the effects of a weaker Euro. Excluding the impact of the weaker Euro, sales from the Company's European-based operations grew 35% in the Second Quarter as a result of increased licensed brand watch sales, further penetration of FOSSIL jewelry that was launched in the first quarter of 2001 and sales in the U.K. by The Avia Watch Company that was acquired in May 2001. Other domestic product sales grew 13% to \$22 million as FOSSIL brand leather goods continued to gain market share and eyewear sales increased as a result of the launch of RELIC eyewear. Additionally, sales from the Company's retail stores grew 27% from additional store openings. Excluding the \$8.3 million sale and the effects of a weaker Euro, the Year To Date Period net sales increased 13% due primarily to increases in sales from the Company's international operations, retail stores and leather business. Net sales from the Company's international businesses benefited from increasing licensed watch product sales and the launch of FOSSIL jewelry. Net sales from the Company's retail stores increased 37% during the Year To Date Period from additional store openings while the Company's leather business grew 27% primarily due to increased handbag sales and increased sales from RELIC leather. The Second Quarter and Year To Date Period increases were offset by a 14% and 10% decline, respectively, in the Company's domestic watch business resulting from a slowdown in

consumer spending and a decrease in retail inventory levels related primarily to the Company's department store customers.

Gross Profit. Gross margins for the Second Quarter increased to 50.6% compared to 49.9% in the Prior Year Quarter while Year To Date Period gross margins decreased to 50.0% compared to 50.8% in the Prior Year YTD Period. Gross margins for both the Second Quarter and the Year To Date Period were favorably impacted from the non-recurrence of the \$8.3 million sale that carried a gross margin lower than the Company's historical consolidated gross margin. Excluding the effects of this sale, gross margins decreased approximately 140 and 180 basis points in the Second Quarter and the Year To Date Period, respectively. These decreases were primarily a result of increased markdowns in the Company's leather and eyewear product divisions and a weaker Euro. The Year To Date Period was further impacted unfavorably by an increase in sales from the Company's leather products business that generates gross margins substantially below the Company's historical consolidated gross margin. Positively impacting gross profit margins for both periods, was an increase in the sales mix of licensed watch and retail store sales that both generate gross margins in excess of the Company's historical consolidated gross margin. Management believes its gross margins will be slightly higher in the second half of 2001 as compared to the second half of 2000 due to a more favorable Euro comparison, based upon current Euro rates, and a continued higher mix of licensed watch and retail store sales.

Operating Expenses. Operating expenses, as a percentage of net sales, increased to 40.3% in the Second Quarter compared to 31.8% in the Prior Year Quarter. For the Year To Date Period, operating expenses as a percentage of sales increased to 38.0% compared to 31.6% in the Prior Year YTD Period. For both the Second Quarter and Year To Date Period, operating expenses increased due to infrastructure costs added primarily in the latter half of fiscal 2000 and costs attributable to the growth in the Company's retail store locations. The infrastructure increases include the addition of key personnel, increased distribution capacity and other costs necessary to support initiatives for future sales growth. Operating expenses, as a percentage of net sales, related to the retail stores are significantly higher than the Company's consolidated average during the first half of the year as retail stores sales are more heavily weighted toward the second half of the year. On a percentage of sales basis, management believes operating expenses in the second half of fiscal 2001 will be less than the corresponding period in the prior year as it begins to anniversary the increases discussed above.

Operating Income. Management believes the Company will achieve a full year operating profit margin in the 16% plus range. Although operating income margins were below this level during the first half of the year, the Company believes earnings will be more heavily back-end weighted due to the significance of the (i) Company's growing retail operations, (ii) weaker Euro on a comparable basis in the first half of fiscal year 2001 and (iii) infrastructure costs added in the latter half of fiscal year 2000.

Other Income (Expense). Other income (expense) increased favorably by approximately \$770,000 during the Second Quarter and \$844,000 during the Year To Date Period. These increases were primarily related to: (i) a one-time fee paid by a customer to the Company for web design consultation and (ii) decreased minority interest expense resulting from the Company's acquisition of additional equity interests in its majority-owned factories.

Liquidity and Capital Resources

The Company's general business operations historically have not required substantial cash needs during the first several months of its fiscal year. Generally, starting in the second quarter the Company's cash needs begin to increase, typically reaching its peak in the September-November time frame. During the Second Quarter, the Company's cash holdings and short-term marketable securities decreased to \$73 million in comparison to \$87 million at the end of Prior Year Quarter. This decrease is primarily related to the Company acquiring in excess of \$30 million of its common stock during the second half of fiscal 2000 and the first quarter of fiscal 2001. Approximately 475,000 shares are still available for repurchase under the previous buyback authorizations.

Accounts receivable and inventory levels increased 10% and 1%, respectively, over last year's comparable quarter. Days sales outstanding increased to 45 days in the Second Quarter compared to 41 days in the previous year quarter. However, when excluding the \$8.3 million sale which occurred and was fully collected in the Prior Year Quarter, days sales outstanding were virtually unchanged at 42 days. Inventory levels remained relatively unchanged, although the Company's retail store inventories increased by approximately \$5 million as a result of additional stores being opened. Excluding the increase from retail stores and inventory associated with the acquisition of The Avia Watch Company in May, inventory levels decreased approximately 6%.

At the end of the Second Quarter, the Company had working capital of \$169 million compared to working capital of \$174 million and \$170 million at the end of the Prior Year Quarter and fiscal 2000 year-end, respectively. The Company had outstanding borrowings of \$4.7 million against its combined \$43 million bank credit facilities at the end of the Second Quarter. The Company anticipates that during September it will spend approximately \$20 million for the acquisition of a new 500,000 square foot distribution facility located near its corporate headquarters. Additionally, from the acquisition date until such time that the distribution center opens (tentatively scheduled for the first quarter 2002) the Company expects to spend approximately \$10 million on related distribution systems and equipment. Management believes that cash flow from operations combined with existing cash on hand and amounts available under its credit facility will be sufficient to satisfy the cash requirements of its new distribution facility and other working capital expenditures for at least the next eighteen months.

Forward-Looking Statements

Included within management's discussion of the Company's operating results, "forward-looking statements" were made within the meaning of the Private Securities Litigation Reform Act of 1995 regarding expectations for 2001. The actual results may differ materially from those expressed by these forward-looking statements. Significant factors that could cause the Company's 2001 operating results to differ materially from management's current expectations include, among other items, significant changes in consumer spending patterns or preferences, competition in the Company's product areas, international in comparison to domestic sales mix, changes in foreign currency valuations in relation to the United States dollar, principally the European Union's, an inability of management to control operating expenses in relation to net sales without damaging the long-term direction of the Company and the risks and uncertainties set forth in the Company's current report on Form 8-K dated March 30, 1999.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As a multinational enterprise, the Company is exposed to changes in foreign currency exchange rates. The Company employs a variety of practices to manage this market risk, including its operating and financing activities and, where deemed appropriate, the use of derivative financial instruments. Forward contracts have been utilized by the Company to mitigate foreign currency risk. The Company's most significant foreign currency risks relate to the Euro. The Company uses derivative financial instruments only for risk management purposes and does not use them for speculation or for trading. There were no significant changes in how the Company managed foreign currency transactional exposures during the Second Quarter and management does not anticipate any significant changes in such exposures or in the strategies it employs to manage such exposures in the near future.

PART II - OTHER INFORMATION

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Company held its annual meeting of stockholders (the "Meeting") on May 24, 2001. At the Meeting, the stockholders voted upon (i) a proposal to elect three (3) Class III directors of the Company to serve for a term of three years ("Proposal 1"); and (ii) a proposed amendment to the 1993 Long-Term Incentive Plan of Fossil to increase the number of shares of common stock that may be made the subject of grants ("Proposal 2"). No other matters were voted on at the Meeting. A total of 29,126,703 shares were represented at the Meeting.

The number of shares that were voted for, and that were withheld from, each of the director nominees in Proposal 1 is as follows:

<u>Director Nominee</u>	<u>For</u>	<u>Withheld</u>
Tom Kartsotis	27,103,513	2,023,190
Jal S. Shroff	27,104,033	2,022,670
Donald J. Stone	27,901,021	1,225,682

The directors whose term of office as a director continued after the Meeting are Kosta Kartsotis, Michael W. Barnes, Richard H. Gundy, Kenneth W. Anderson, Alan J. Gold, Junichi Hattori and Michael Steinberg.

The number of shares that were voted for, against and abstained from Proposal 2 is as follows:

<u>For</u>	<u>Against</u>	<u>Abstain</u>
21,646,654	7,467,788	12,261

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

4.1 ⁽¹⁾ Third Amendment to the Fossil, Inc. 1993 Long-Term Incentive Plan

10.1 Agreement for the Sale and Purchase of the Avia Watch Company Limited between Roventa-Henex S.A. and Fossil (UK) Holdings Limited and Fossil, Inc. dated May 4, 2001.

⁽¹⁾ Management contract or compensatory plan or arrangement.

(b) Reports on Form 8-K

No reports on Form 8-K were filed during the period covered by this Report.

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.

FOSSIL, INC.

Date: August 20, 2001

Mike L. Kovar
Senior Vice President and Chief Financial Officer
(Principal financial and accounting officer duly
authorized to sign on behalf of Registrant)

EXHIBIT INDEX

<u>Exhibit Number</u>	<u>Document Description</u>
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(1)	Management contract or compensatory plan or arrangement.