

CSS INDUSTRIES INC
Form 10-K
June 05, 2018
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark one)

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

For the fiscal year ended March 31, 2018

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 1-2661

CSS INDUSTRIES, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

13-1920657

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

450 Plymouth Road, Suite 300, Plymouth Meeting, PA 19462

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (610) 729-3959

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

Title of each class	Name of each exchange on which registered
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Common Stock, \$.10 par value	New York Stock Exchange
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Securities registered pursuant to Section 12(g) of the Act: None

(Title of class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☒

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such period that the registrant was required to submit and post such files). Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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 ☒
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 ☒

The aggregate market value of the voting stock held by non-affiliates of the registrant is \$255,661,557. Such aggregate market value was computed by reference to the closing price of the common stock of the registrant on the New York Stock Exchange on September 29, 2017, being the last trading day of the registrant's most recently completed second fiscal quarter. Such calculation excludes the shares of common stock beneficially owned at such date by certain directors and officers of the registrant, as described under the section entitled "Ownership of CSS Common Stock" in the proxy statement to be filed by the registrant for its 2018 Annual Meeting of Stockholders. In making such calculation, registrant does not determine the affiliate or non-affiliate status of any holders of the shares of common stock for any other purpose.

At June 1, 2018, there were outstanding 9,119,746 shares of common stock.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement for its 2018 Annual Meeting of Stockholders are incorporated by reference into Part III of this Form 10-K.

CSS INDUSTRIES, INC.
FORM 10-K
FOR THE FISCAL YEAR ENDED MARCH 31, 2018
INDEX

	Page
<u>PART I</u>	
Item 1. <u>Business</u>	<u>1</u>
Item 1A. <u>Risk Factors</u>	<u>4</u>
Item 1B. <u>Unresolved Staff Comments</u>	<u>11</u>
Item 2. <u>Properties</u>	<u>12</u>
Item 3. <u>Legal Proceedings</u>	<u>12</u>
Item 4. <u>Mine Safety Disclosures</u>	<u>12</u>
<u>PART II</u>	
Item 5. <u>Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	<u>13</u>
Item 6. <u>Selected Financial Data</u>	<u>15</u>
Item 7. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>16</u>
Item 7A. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>25</u>
Item 8. <u>Financial Statements and Supplementary Data</u>	<u>26</u>
Item 9. <u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	<u>59</u>
Item 9A. <u>Controls and Procedures</u>	<u>59</u>
Item 9B. <u>Other Information</u>	<u>61</u>
<u>PART III</u>	
Item 10. <u>Directors, Executive Officers and Corporate Governance</u>	<u>62</u>
Item 11. <u>Executive Compensation</u>	<u>62</u>
Item 12. <u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>62</u>
Item 13. <u>Certain Relationships and Related Transactions, and Director Independence</u>	<u>62</u>
Item 14. <u>Principal Accounting Fees and Services</u>	<u>62</u>
<u>PART IV</u>	
Item 15. <u>Exhibits and Financial Statement Schedules</u>	<u>63</u>
<u>Signatures</u>	<u>68</u>

PART I

Item 1. Business.

General

CSS Industries, Inc. ("CSS" or the "Company") is a creative consumer products company, focused on the seasonal, gift and craft categories. For these design-driven categories, the Company engages in the creative development, manufacture, procurement, distribution and sale of our products with an omni-channel approach focused primarily on mass market retailers.

Seasonal The seasonal category includes gift packaging items such as ribbon, bows, greeting cards, wrapping paper, bags, boxes, tags and gift card holders, in addition to specific holiday-themed decorations, accessories, and activities, such as Easter egg dyes and novelties and Valentine's Day classroom exchange cards. These products are sold to mass market retailers, and production forecasts for these products are generally known well in advance of shipment.

Gift The gift category (formerly described by the Company as its celebrations category) includes products designed to celebrate certain life events or special occasions, such as weddings, birthdays, anniversaries, graduations, or the birth of a child. Products include ribbons and bows, floral accessories, infant products, journals, gift card holders, all occasion boxed greeting cards, memory books, scrapbooks, stationery, stickers and other items that commemorate life's celebrations. Products in this category are primarily sold into mass and specialty retailers, floral and packaging wholesalers and distributors, and are generally ordered on a replenishment basis throughout the year.

Craft The craft category includes ribbons, trims, buttons, sewing patterns, knitting needles, needle arts and kids' crafts. These products are sold to mass market and specialty retailers, and are generally ordered on a replenishment basis throughout the year.

CSS' product breadth provides its retail customers the opportunity to use a single vendor for much of their seasonal, gift and craft product requirements. A substantial portion of CSS' products are manufactured and packaged in the United States and warehoused and distributed from facilities in the United States, the United Kingdom and Australia, with the remainder sourced from foreign suppliers, primarily in Asia. The Company also has a manufacturing facility in India that produces certain craft products, including trims, braids and tassels, and also has a distribution facility in India. The Company's products are sold to its customers by national and regional account sales managers, sales representatives, product specialists and by a network of independent manufacturers' representatives. CSS maintains purchasing offices in Hong Kong and China to administer Asian sourcing opportunities.

A key aspect of the Company's strategy is to reposition its portfolio primarily through acquisitions within the categories that the Company currently operates. The highly fragmented nature of the categories in which the Company operates creates opportunities to grow through acquisition. As a result, the Company actively meets with craft, gift and seasonal companies to assess potential fit against our pre-defined parameters, seeking to deploy its cash to grow through acquisition.

The overall objective of the Company is to grow profitable sales and improve return on invested capital ("ROIC") through five strategic pillars. These strategic pillars include:

- *Defend the base business - Design, product innovation, category leadership
- *Identify adjacent product categories with a focus on brands - Focus on fragmented markets, brands, omni-channel
- *Build an omni-channel business model - Dedicated resources, leverage technology
- *Improve ROIC by maximizing margins while minimizing capital investment - Fix underperforming product lines, focus on working capital
- *Build a collaborative, dynamic One CSS culture - Communication, accountability, talent infusion

Principal Products CSS designs, manufactures, procures, distributes and sells a broad range of craft and gift consumer products. Craft and gift consumer products include ribbons and bows, trims, buttons, sewing patterns, knitting needles, needle arts, kids' crafts, floral accessories, infant products, journals, gift card holders, all occasion boxed greeting cards, memory books, scrapbooks, stationery, stickers and other gift and craft items, sold to its mass market, craft, specialty and floral retail and wholesale distribution customers. CSS also designs, manufactures, procures, distributes and sells a broad range of seasonal consumer products primarily through the mass market distribution channel.

Christmas products include packaging ribbons and bows, boxed greeting cards, gift wrap, gift bags, gift boxes, gift tags, gift card holders, tissue paper and decorations. CSS' Valentine's Day product offerings include classroom exchange Valentine's Day cards and other related

Valentine's Day products, while its Easter product offerings include Dudley's® brand of Easter egg dyes and related Easter seasonal products. Its back-to-school products include teachers' aids and other learning oriented products to the education market sold through mass market retailers, school supply distributors and teachers' stores.

Key brands include Paper Magic®, Berwick®, Offray®, C.R. Gibson®, McCall's®, Butterick®, Kwik Sew®, Vogue Patterns®, Markings®, Stepping Stones®, Tapestry®, Seastone®, Dudley's®, Eureka®, Stickerfitti®, Favorite Findings®, La Mode®, Simplicity®, Wrights®, Boye®, Dimensions® and Perler®.

CSS operates nineteen manufacturing and/or distribution facilities located in Pennsylvania, Maryland, New Hampshire, South Carolina, Alabama, Illinois, Kansas, the United Kingdom, Australia and India. A description of the Company's product lines and related manufacturing and/or distribution facilities is as follows:

Ribbon and bows are primarily manufactured and warehoused in eight facilities located in Pennsylvania, Maryland, South Carolina and Alabama. The manufacturing process is vertically integrated. Non-woven ribbon and bow products are primarily made from polypropylene resin, a petroleum-based product, which is mixed with color pigment, melted and pressed through an extruder. Large rolls of extruded film go through various combinations of manufacturing processes before being made into bows or packaged on ribbon spools or reels as required by various markets and customers. Woven fabric ribbons are manufactured domestically or imported from Mexico and Asia. Imported woven products are either narrow woven or converted from bulk rolls of wide width textiles. Domestic woven products are narrow woven.

Infant products, journals, educational products, memory books, scrapbooks, stationery, and other gift items are imported from Asian manufacturers and warehoused and distributed from two distribution facilities in Alabama. Floral accessories, including pot covers, foil, waxed tissue, shred, aisle runners, corsage bags and other paper and film products, are manufactured in a facility located in New Hampshire or imported from Mexico. Manufacturing includes gravure and flexo printing, waxing and converting. Products are warehoused and distributed from a distribution facility in Pennsylvania.

Sewing patterns are purchased and distributed from a third party printer and are also manufactured and distributed from a facility located in Kansas. Sewing patterns are also warehoused and distributed from two distribution facilities in the United Kingdom and two distribution facilities in Australia.

Certain craft items, including trims, braids and tassels, are manufactured and distributed from two facilities in India. Other products including, but not limited to, buttons, knitting needles, needle arts, kids crafts, boxed greeting cards, gift tags, gift card holders, gift bags, gift wrap, decorative tissue paper, classroom exchange Valentine's Day products, Easter products, and decorations are produced to the specifications of CSS and are imported primarily from Asian manufacturers.

During our 2018 fiscal year, CSS experienced no material difficulties in obtaining raw materials or finished goods from suppliers.

Intellectual Property Rights CSS has a number of copyrights, patents, tradenames, trademarks and intellectual property licenses which are used in connection with its products. Substantially all of its designs and artwork are protected by copyright. Intellectual property license rights which CSS has obtained are viewed as especially important to the success of its classroom exchange Valentine's Day cards and stickers. It is CSS' view that its operations are not dependent upon any individual patent, tradename, trademark, copyright or intellectual property license. The collective value of CSS' intellectual property is viewed as substantial, and CSS seeks to protect its rights in all patents, copyrights, tradenames, trademarks and intellectual property licenses.

Sales and Marketing Most of CSS' products are sold in the United States and Canada by national and regional account sales managers, sales representatives, product specialists and by a network of independent manufacturers' representatives. CSS maintains permanent showrooms in Pennsylvania, Georgia, Arkansas, Ohio, Tennessee, Texas, Hong Kong and Australia where buyers for major retail customers will typically visit for a presentation and review of the new lines. Products are also displayed and presented in showrooms maintained by various independent manufacturers' representatives in major cities in the United States and Canada. Relationships are developed with key retail customers by CSS sales personnel and independent manufacturers' representatives. Social stationery products are sold by a national organization of sales representatives that specialize in the gift and specialty channel, as well as by key account representatives. Craft ribbon and bow products are also sold through sales representatives or independent manufacturers' representatives to wholesale distributors and independent small retailers who serve the floral, craft and

retail packaging trades. The Company also sells custom products to private label customers, to other social expression companies, and to converters of the Company's ribbon products. Custom products are sold by both independent manufacturers' representatives and CSS sales managers.

Customers are generally mass market retailers, discount department stores, specialty chains, warehouse clubs, drug and food chains, dollar stores, office supply stores, independent card, gift and floral shops and retail teachers' stores. Net sales to Walmart Stores, Inc. and its affiliates accounted for approximately 25% of total net sales during fiscal 2018. No other customer accounted for 10% or more of the Company's net sales in fiscal 2018. Our ten largest customers, which include mass market retailers, warehouse clubs and national drug store chains, accounted for approximately 61% of our sales in our 2018 fiscal year. Approximately 66% of the Company's sales are attributable to gift and craft products with the remainder attributable to seasonal (Christmas, Valentine's Day, Easter and back to-school) products. Approximately 24% of CSS' sales relate to the Christmas season. Seasonal products are generally designed and marketed beginning up to 18 to 20 months before the holiday event and manufactured during an eight to ten month production cycle. Due to these long lead time requirements, timely communication with third party factories, licensors, customers and independent manufacturers' representatives is critical to the timely production of seasonal products. Sales terms for our seasonal products do not generally require payment until just before or just after the holiday, in accordance with industry practice. CSS products, with some customer specific exceptions, are not sold under guaranteed or return privilege terms. The Company has certain limited products, primarily sewing patterns, that are on consignment at mass market retailers and the Company recognizes the sale as products are sold to end consumers at point-of-sale terminals.

Competition among retailers in the sale of the Company's products to end users is intense. CSS seeks to assist retailers in developing merchandising programs designed to enable the retailers to meet their revenue and profit objectives while appealing to their consumers' tastes. These objectives are met through the development and manufacture of custom configured and designed products and merchandising programs. CSS' years of experience in merchandising program development and product quality are key competitive advantages in helping retailers meet their objectives. Competition CSS competes with various domestic and foreign companies in each of its seasonal, gift and craft categories. Some of our competitors are larger and have greater resources than the Company while many are smaller, private companies that we compete with across our product lines. CSS believes its products are competitively positioned in their primary markets. Since competition is based primarily on category knowledge, timely delivery, creative design, price and, with respect to seasonal products, the ability to serve major retail customers with single, combined product shipments for each holiday event, CSS believes that its focus on products, combined with consistent service levels, allows it to compete effectively in its core markets.

Backlog Production forecasts for products within our seasonal category are generally known well in advance of shipment. Orders for products within our gift and craft categories are generally ordered on a just-in-time replenishment basis by our customers and an order backlog does not typically exist, except when major program resets occur.

The Company's fiscal year ends on March 31. References to a particular year refer to the fiscal year ending in March of that year. For example, fiscal 2018 refers to the fiscal year ended March 31, 2018.

Employees

At June 1, 2018, approximately 2,000 persons were employed by CSS (increasing to approximately 2,075 as seasonal employees are added). The Company believes that relationships with its employees are good.

With the exception of the bargaining unit at the ribbon manufacturing facility in Hagerstown, Maryland, which totaled 80 employees as of June 1, 2018, CSS employees are not represented by labor unions. Because of the seasonal nature of certain of its businesses, the number of production employees fluctuates during the year. The collective bargaining agreement with the labor union representing the Hagerstown-based production and maintenance employees remains in effect until December 31, 2020. Historically, we have been successful in renegotiating expiring agreements without any disruption of operating activities.

Acquisitions

The Company will continue to build on existing relationships with seasonal, gift and craft customers by expanding and diversifying its product lines and thereby growing its presence in the largest retailers in North America. This includes both capitalizing on opportunities for organic growth in existing businesses as well as acquiring companies which fit into appropriate acquisition parameters. We actively meet with seasonal, gift and craft companies to review and assess potential acquisition targets.

On November 3, 2017, the Company completed the acquisition of substantially all of the net assets and business of Simplicity Creative Group ("Simplicity") from Wilton Brands LLC ("Wilton") for a total consideration of \$69,617,000 and transaction costs of approximately \$3,411,000. Simplicity is a leading provider of home sewing patterns, decorative trims, knitting and crocheting tools, needle arts and kids' crafts products under the Simplicity®, Wrights®, Boye®, Dimensions®, and

Perler® brand names. Simplicity's products are sold to mass-market retailers, specialty fabric and craft chains, wholesale distributors and online customers. The Company primarily financed the acquisition with borrowings of \$60,000,000 under its revolving credit facility and has recorded a working capital adjustment due to Wilton of \$2,500,000, which is recorded in other current liabilities in the accompanying consolidated balance sheet and was paid on April 4, 2018. A portion of the purchase price is being held in escrow for certain post closing adjustments and indemnification obligations. The acquisition was accounted for using the acquisition method and the excess of cost over the fair market value of the net tangible and identifiable intangible assets acquired of \$9,642,000 was recorded as goodwill. This goodwill was subsequently written off as a result of the Company's annual impairment testing performed in the fourth quarter of fiscal 2018 as further described in Note 3 to the consolidated financial statements. On December 13, 2016, the Company completed the acquisition of substantially all of the net assets and business of The McCall Pattern Company and certain affiliated subsidiaries ("McCall"), for approximately \$13,914,000 in cash, plus transaction costs of approximately \$1,484,000. McCall designs, manufactures, and sells home sewing patterns under the McCall's®, Butterick®, Kwik Sew® and Vogue Patterns® brand names. McCall is a leading provider of home sewing patterns, selling to mass market retailers, specialty fabric and craft chains, and wholesale distributors. A portion of the purchase price is being held in escrow for certain post closing adjustments and indemnification obligations. The acquisition was accounted for using the acquisition method and resulted in a bargain purchase due to the fair value of the net assets acquired of approximately \$33,528,000 exceeding the amount paid. In connection with this bargain purchase, the Company recorded a gain of approximately \$19,614,000 in the consolidated statements of operations in the fiscal year ended March 31, 2017.

On July 8, 2016, a subsidiary of the Company completed the acquisition of substantially all of the assets of Lawrence Schiff Silk Mills, Inc. ("Schiff") for \$1,125,000 in cash. Schiff was a leading U.S. manufacturer and distributor of narrow woven ribbon prior to its April 2016 Chapter 11 bankruptcy filing. The acquisition was accounted for using the acquisition method and resulted in a bargain purchase due to the fair value of the net assets acquired of approximately \$1,501,000 exceeding the amount paid. In connection with this bargain purchase, the Company recorded a gain of approximately \$376,000 in the consolidated statements of operations in the fiscal year ended March 31, 2017.

On February 2, 2016, a subsidiary of the Company completed the acquisition of substantially all of the net assets and business of Blumenthal Lansing Company, LLC ("Blumenthal") for approximately \$19,626,000 in cash, including transaction costs of approximately \$81,000. The Company also incurred costs of approximately \$1,028,000 in fiscal 2016, primarily related to severance. Blumenthal was a leading provider of buttons to the sewing and craft markets in the United States, selling to mass market retailers and wholesale distributors that service independent retail stores. The acquisition was accounted for using the acquisition method, and \$4,017,000, which is the excess of cost over fair value of the net tangible and identifiable intangible assets acquired, was recorded as goodwill. This goodwill was subsequently written off as a result of the Company's annual impairment testing performed in fiscal 2018 as further described in Note 3 to the consolidated financial statements.

SEC Filings

The Company's Internet address is www.cssindustries.com. Through its website, the following filings are made available free of charge as soon as reasonably practicable after they are electronically filed with or furnished to the Securities and Exchange Commission: its annual report on Form 10-K, its quarterly reports on Form 10-Q, its current reports on Form 8-K and any amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934.

Item 1A. Risk Factors.

You should carefully consider each of the risk factors we describe below, as well as other factors described in this annual report on Form 10-K and elsewhere in our SEC filings.

Our results of operations fluctuate on a seasonal basis, and quarter to quarter comparisons may not be a good indicator of our performance. Seasonal demand fluctuations may adversely affect our cash flow and our ability to sell our products.

Approximately 66% of the Company's sales are attributable to products within our gift and craft categories, with the remainder attributable to products in the seasonal category. Approximately 24% of our sales relate to the Christmas season. The seasonal nature of our business has historically resulted in lower sales levels and operating losses in our

first and fourth quarters, and higher sales levels and operating profits in our second and third quarters. As a result, our quarterly results of operations fluctuate during our fiscal year, and a quarter to quarter comparison is not a good indication of our performance or how we will perform in the future. For example, our overall results of operations in the future may fluctuate substantially based on seasonal demand for our products. Such variations in demand could have a material adverse effect on the timing of cash flow and therefore our ability to meet our obligations with respect to our debt and other financial commitments. Seasonal

fluctuations also affect our inventory levels. We must carry significant amounts of inventory, especially before the Christmas retail selling period. If we are not successful in selling the inventory during the relevant period, we may have to sell the inventory at significantly reduced prices, or we may not be able to sell the inventory at all.

We rely on a few mass market retailers, warehouse clubs and national drug store chains for a significant portion of our sales. The loss of sales, or a significant reduction of sales, to one or more of our large customers may adversely affect our business, results of operations and financial condition. Past and future consolidation within the retail sector also may lead to reduced profit margins, which may adversely affect our business, results of operations and financial condition.

A few of our customers are material to our business and operations. Our sales to Walmart Stores, Inc. and its affiliates accounted for approximately 25% of our sales during our 2018 fiscal year. No other single customer accounted for 10% or more of our sales in fiscal 2018. Our ten largest customers, which include mass market retailers, warehouse clubs and national drug store chains, accounted for approximately 61% of our sales in our 2018 fiscal year. Our business depends, in part, on our ability to identify and define product and market trends, and to anticipate, understand and react to changing consumer demands in a timely manner. There can be no assurance that our large customers will continue to purchase our products in the same quantities that they have in the past. The loss of sales, or a significant reduction of sales, with one or more of our large customers, including without limitation a loss or significant reduction in sales resulting from our failure or inability to comply with one or more of any of our customers' sourcing requirements, may adversely affect our business, results of operations and financial condition. Further, in recent years there has been consolidation among our retail customer base. As the retail sector consolidates, our customers become larger, and command increased leverage in negotiating prices and other terms of sale of our products, including credits, discounts, allowances and other incentive considerations to these customers. Past and future consolidation may lead to reduced profit margins, which may adversely affect our business, results of operations and financial condition.

A portion of our products, primarily sewing patterns, are sold on a consignment basis by third party consignment sellers, including certain mass market retailers. Because of the nature of the consignment arrangement, we may be adversely affected if third party consignment sellers, including mass market retailers, experience difficulties in recording sales of the products to end consumers, or in accounting for, or paying us for, the sales of such products. Additionally, while the consigned products are physically stored with third parties, including third party consignment sellers, we do not have custody or control of such products, and the consigned products are subject to damage or loss, including, but not limited to, theft. Any failure or inability by third parties, including third party consignment sellers, to appropriately manage the consignment arrangement may adversely affect our business, results of operations and financial condition.

A portion of our products, primarily sewing patterns, are sold on a consignment basis by third party consignment sellers, including certain mass market retailers. Under the consignment arrangement, the applicable products are physically stored at third party locations, including mass market retailer store locations, and we retain title to the consigned products until such products are purchased by an end consumer. We recognize the sale of such consigned products at the time that the products are sold to the end consumer, as recorded at the applicable seller's point-of-sale terminals. Under this arrangement, we are subject to the ability of third party consignment sellers, including mass market retailers, to appropriately record the sales of our consigned products to end consumers, and to appropriately account for, and pay us for, such recorded sales. The failure or inability of third party consignment sellers, including mass market retailers, to record sales of our consigned products, and to appropriately account for, and pay us for, such recorded sales may adversely affect our business, results of operations and financial condition. Additionally, while our consigned products are physically stored with third parties, including third party consignment sellers, we do not have custody or control of such products, and the consigned products are subject to damage or loss, including, but not limited to, theft. There can be no assurance that third parties, including third party consignment sellers, will appropriately handle, monitor, secure or protect our consigned products, and any failure or inability to do so may adversely affect our business, results of operations and financial condition.

Increases in raw material and energy costs, resulting from general economic conditions, acts of nature, such as hurricanes, earthquakes or pandemics, acts of war, threats of war, terrorism, civil unrest, or other factors, may raise our cost of goods sold and adversely affect our business, results of operations and financial condition.

Paper and petroleum-based materials are essential in the manufacture of some of our products, such as our stationery and plastic decorative ribbons products, and the cost of such materials is significant to our cost of goods sold. Energy costs, especially fuel costs, also are significant expenses in the production and delivery of our products. Increased costs of raw materials or energy resulting from general economic conditions, acts of nature, such as hurricanes, earthquakes or pandemics, acts of war, threats of war, terrorism, civil unrest, or other factors, may result in declining margins and operating results if market conditions prevent us from passing these increased costs on to our customers through timely price increases on our products.

Risks associated with our use of foreign suppliers may adversely affect our business, results of operations and financial condition.

For a large portion of our product lines, with the exception of our decorative ribbon and bow product lines and sewing patterns, we use foreign suppliers to manufacture a significant portion of our products. Approximately 58% of our sales in fiscal 2018 were related to products sourced from foreign suppliers. Our use of foreign suppliers exposes us to risks inherent in doing business outside of the United States, including risks associated with foreign currency fluctuations, transportation costs and delays or disruptions, difficulties in maintaining and monitoring quality control (including without limitation risks associated with defective products), enforceability of agreed upon contract terms, compliance with existing and new United States and foreign laws and regulations, such as the United States Foreign Corrupt Practices Act and legislation and regulations relating to imported products, costs relating to the imposition or retrospective application of antidumping and countervailing duties or other trade-related sanctions on imported products, economic, civil or political instability, acts of war, threats of war, terrorism, civil unrest, labor-related issues, such as labor shortages or wage disputes or increases, international public health issues, and restrictions on the repatriation of profits and assets.

Increased overseas sourcing by our competitors and our customers may reduce our market share and profit margins, adversely affecting our business, results of operations and financial condition.

We have relatively high market share in many of our seasonal product categories. Most of our product markets have shown little or no growth, and some of our product markets have declined in recent years, and we continue to confront significant cost pressure as our competitors source certain products from overseas and certain customers increase direct sourcing from overseas factories. Increased overseas sourcing by our competitors and certain customers may result in a reduction of our market share and profit margins, adversely affecting our business, results of operations and financial condition.

Difficulties encountered by our key customers may cause them to reduce their purchases from us and/or increase our exposure to losses from bad debts, and adversely affect our business, results of operations and financial condition. Many of our largest customers are national and regional retail chains. The retail channel in the United States has experienced significant shifts in market share among competitors in recent years, including as a result of the presence and continued growth of e-commerce retailers. Any current or future economic slowdown, slow economic recovery, or uncertain economic outlook could further adversely affect our key customers. Our business, results of operations and financial condition may be adversely affected if our customers file for bankruptcy protection and/or cease doing business, significantly reduce the number of stores they operate, significantly reduce their purchases from us, do not pay us for their purchases, or if their payments to us are delayed or reduced because of bankruptcy or other factors beyond our control.

Our inability to effectively develop, manufacture, procure, distribute and sell our products with an omni-channel approach may adversely affect our business, results of operations and financial condition.

The retail channel in the United States is rapidly evolving, and consumers are increasingly embracing online shopping, including through mobile commerce applications. Many of our retail customers are experiencing a shift of their total consumer expenditures from sales at physical retail locations to sales on digital platforms. Our retail customers expect us, as a product supplier, to assist them to deliver a seamless omni-channel shopping experience.

Additionally, our strategy includes a greater focus on our own direct-to-consumer online shopping opportunities. We continue to invest in e-commerce technology, including the development of our digital platforms and mobile commerce applications. Our business, results of operations and financial condition may be adversely affected if we are unable to effectively develop, manufacture, procure, distribute and sell our products with an omni-channel approach.

Our business, results of operations and financial condition may be adversely affected by volatility in the demand for our products.

Our success depends on the sustained demand for our products. Many factors affect the level of consumer spending on our products, including, among other things, general business conditions, interest rates, the availability of consumer credit, taxation, the effects of war, terrorism or threats of war, civil unrest, fuel prices, consumer demand for our products based upon, among other things, consumer trends and the availability of alternative products, and consumer confidence in future economic conditions. A decline in economic activity in the United States or other regions of the world, a slow economic recovery, or an uncertain outlook, in addition to adversely affecting our customers, could adversely affect our business, results of operations and financial condition because of, among other things, reduced consumer spending on discretionary items, including our products. We also routinely utilize new artwork, designs or licensed intellectual property in connection with our products, and our inability to design, select, procure, maintain or sell consumer-desired artwork, designs or

licensed intellectual property could adversely affect the demand for our products, which could adversely affect our business, results of operations and financial condition.

Our business, results of operations and financial condition may be adversely affected if we are unable to compete successfully against our competitors.

Our success depends in part on our ability to compete against our competitors in our highly competitive markets. Our competitors, including domestic businesses, foreign manufacturers who market directly to our customer base, and importers of products, may be able to offer similar products with more favorable pricing, servicing and/or terms of sale or may be able to provide products that more readily meet customer requirements or consumer preferences. Our inability to successfully compete against our competitors could adversely affect our business, results of operations and financial condition.

Our business, results of operations and financial condition may be adversely affected if we are unable to hire and retain sufficient qualified personnel.

Our success depends, to a substantial extent, on the ability, experience and performance of our senior management. In order to hire and retain qualified personnel, including our senior management team, we seek to provide competitive compensation programs. Our inability to retain our senior management team, or our inability to attract and retain qualified replacement personnel, may adversely affect us. We also regularly hire a large number of seasonal employees. Any difficulty we may encounter in hiring seasonal employees may result in significant increases in labor costs, which may have an adverse effect on our business, results of operations and financial condition.

Employee benefit costs may adversely affect our business, results of operations and financial condition.

We seek to provide competitive employee benefit programs to our employees. Employee benefit costs, such as healthcare costs for our eligible and participating employees, may increase significantly at a rate that is difficult to forecast, in part because of the current and/or future impact of federal healthcare legislation on our employer-sponsored medical plans. Higher employee benefit costs could have an adverse effect on our business, results of operations and financial condition.

Our acquisition strategy involves risks, and difficulties in integrating potential acquisitions may adversely affect our business, results of operations and financial condition.

We regularly evaluate potential acquisition opportunities to support, strengthen and grow our business. In fiscal 2018, we completed the acquisition of substantially all of the business and net assets of Simplicity. In fiscal 2017, we completed the acquisitions of substantially all of the businesses and net assets of McCall and Schiff and in fiscal 2016, we completed the acquisition of substantially all of the business and net assets of Blumenthal. We cannot be sure that we will be able to locate suitable acquisition candidates, acquire possible acquisition candidates, acquire such candidates on commercially reasonable terms, or integrate acquired businesses successfully. Future acquisitions may require us to incur debt and contingent liabilities, which may adversely affect our business, results of operations and financial condition. The process of integrating acquired businesses into our existing operations may result in operating, contract and supply chain difficulties, such as the failure to retain customers or management personnel. Also, prior to our completion of any acquisition, we could fail to discover liabilities of the acquired business for which we may be responsible as a successor owner or operator in spite of any investigation we may make prior to the acquisition. Such difficulties may divert significant financial, operational and managerial resources from our existing operations, and make it more difficult to achieve our operating and strategic objectives. The diversion of management attention, particularly in a difficult operating environment, may adversely affect our business, results of operations and financial condition.

Our strategy to continuously review the efficiency, productivity and competitiveness of our business may result in our decision to divest or close selected operations. Any divestiture or closure involves risks, and decisions to divest or close selected operations may adversely affect our business, results of operations and financial condition.

We regularly evaluate the efficiency, productivity and competi