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NAUTILUS, INC.

Form 10-K

March 06, 2018

false--12-31FY20172017-12-3110-K0001078207YesAccelerated FilerNAUTILUS, INC.

NoNoP2Y10001000P30D2100014000007500000075000000308250003030500030825000303050000.150.100.150.101700050

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**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 December 31, 2017

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 (I.R.S. Employer
incorporation or organization) 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)

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

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Common Stock, no par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None.

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 shorter 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.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting 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
(do not check if a 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 Act). Yes No

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the last sales price (\$18.90) as reported on the New York Stock Exchange as of the last business day of the registrant's most recently completed second fiscal quarter (June 30, 2017) was \$567,409,298.

The number of shares outstanding of the registrant's common stock as of February 28, 2018 was 30,327,978 shares.

Documents Incorporated by Reference

The registrant has incorporated by reference into Part III of this Form 10-K portions of its Proxy Statement for its 2018 Annual Meeting of Shareholders.

NAUTILUS, INC.
2017 FORM 10-K ANNUAL REPORT

PART I

Item 1. <u>Business</u>	<u>1</u>
Item 1A. <u>Risk Factors</u>	<u>6</u>
Item 1B. <u>Unresolved Staff Comments</u>	<u>12</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>13</u>

PART II

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>28</u>
Item 8. <u>Financial Statements and Supplementary Data</u>	<u>29</u>
Item 9. <u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	<u>64</u>
Item 9A. <u>Controls and Procedures</u>	<u>64</u>
Item 9B. <u>Other Information</u>	<u>65</u>

PART III

Item 10. <u>Directors, Executive Officers and Corporate Governance</u>	<u>65</u>
Item 11. <u>Executive Compensation</u>	<u>65</u>
Item 12. <u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>65</u>
Item 13. <u>Certain Relationships and Related Transactions, and Director Independence</u>	<u>66</u>
Item 14. <u>Principal Accounting Fees and Services</u>	<u>66</u>

PART IV

Item 15. <u>Exhibits and Financial Statement Schedules</u>	<u>66</u>
Item 16. <u>Form 10-K Summary</u>	<u>69</u>
<u>Signatures</u>	<u>69</u>

Table of Contents

PART I

Forward-Looking Statements

This Annual Report on Form 10-K 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. The forward-looking statements in this report include, without limitation: our prospects, resources or capabilities; current or future financial trends; anticipated future operating results; future plans for introduction of new products; anticipated demand for our new and existing products; maintenance of appropriate inventory levels; growth in revenues and profits; leverage of operating expenses; future revenues from licenses of our intellectual property; results of increased media investment in the Direct segment; continued improvement in operating margins; expectations for increased research and development expenses; anticipated capital expenditures; fluctuations in net sales due to seasonality; and our ability to continue to fund our operating and capital needs for the following twelve-month period. Forward-looking statements also include any statements related to our expectations regarding future business and financial performance or conditions, anticipated sales growth across markets, distribution channels and product categories, expenses and gross margins, profits or losses, losses from discontinued operations, settlements of warranty obligations, the anticipated outcome of litigation to which we are a party, new product introductions, financing and working capital requirements and 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 the risks described in Part I, Item 1A of this report and in other reports we file with the Securities and Exchange Commission. 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.

Item 1. Business

OVERVIEW

Founded in 1986, Nautilus, Inc. and subsidiaries (collectively, "Nautilus" or the "Company") is a consumer fitness products company headquartered in Vancouver, Washington and incorporated in the State of Washington in January 1993. We are committed to providing innovative, quality solutions to help people achieve their fitness goals through 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 and commercial use, primarily in the U.S. and Canada, but also in international markets outside North America. 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 companies to reach consumers in both the home use, as well as commercial use, markets in the U.S. and internationally. We also derive a portion of our revenue from the licensing of our brands and intellectual property.

BUSINESS STRATEGY

We are focused on developing and marketing consumer fitness equipment and related products to help people enjoy healthier lives. Our products are targeted to meet the needs of a broad range of consumers, including fitness enthusiasts and individuals who are seeking the benefits of regular exercise. We have diversified our business by

expanding our portfolio of high quality fitness equipment into multiple product lines utilizing our well-recognized brand names. We are focused on consumer markets and specialty and commercial distribution channels, and view the continual innovation of our product offerings as a key aspect of our business strategy. We regularly refresh our existing product lines with new technologies and finishes, and focus significant effort and resources on the development or acquisition of innovative new fitness products for introduction to the marketplace at periodic intervals.

Our strategies incorporate the individual characteristics of our Direct and Retail businesses. Our Direct business focuses on: (i) the development of, or acquisition of rights to, unique, branded products; (ii) the application of creative, cost-effective ways to communicate the benefits of their use; and (iii) making various payment options available to our customers. We are particularly attentive to Direct business metrics that provide feedback regarding the effectiveness of our media marketing programs and attractiveness of third-party consumer financing programs.

Table of Contents

In our Retail business, we strive to develop long-term relationships with key retailers of sports or fitness equipment. The primary objectives of our Retail business are (i) to offer a selection of innovative, unique products at key price-points to capture market share; and (ii) to utilize the strength of our brands and long-standing customer relationships to secure more floor space with our Retail customers for our products, as well as support efforts to gain share in multi-user environments.

Our long-term strategy involves:

- Creatively marketing our equipment, both directly to consumers and through our Retail customers, while leveraging our well-known brand names;
- Enhancing our product lines by designing fitness equipment that meets or exceeds the high expectations of our customers;
- Utilizing our strengths in product engineering to reduce product costs;
- Continuing our investment in research and development activities aimed at acquiring or creating new technologies;
- Increasing our international Retail sales and distribution; and
- Maximizing available royalty revenues from the licensing of our brands and intellectual property.

PRODUCTS

We market quality cardiovascular and strength fitness products that cover a broad range of price points and features. Our products are designed for home use and multi-user environments by individuals with varying exercise needs. From the person who works out occasionally to the serious athlete, we have products that will help them achieve their fitness objectives.

• **Nautilus®** is our corporate umbrella brand and is also used to differentiate certain specialized cardio, treadmills, ellipticals and bike products.

• Our **Bowflex®** brand represents a highly-regarded line of fitness equipment comprised of both cardio and strength products, including the Max Trainer®, TreadClimber®, and HVT® specialized cardio machines, PowerRod® and Revolution® home gyms and SelectTech® dumbbells.

• Our **Octane Fitness®** brand is known for its innovation around low-impact cardio products, including the perfection of the traditional elliptical machine, along with the creation of new categories of exercise, including the xRide® recumbent elliptical, the LateralX® elliptical, and the Zero Runner®.

• Our **Schwinn®** brand is known for its popular line of exercise bikes, including the Airdyne®, as well as Schwinn-branded treadmills and ellipticals.

• Our **Universal®** brand, one of the oldest and most recognized names in the fitness industry, currently offers a line of kettlebell weights and weight benches.

We generally differentiate the product models offered in our Direct and Retail sales channels. Currently, our Max Trainer®, TreadClimber®, and HVT® product lines are offered for sale primarily through our Direct sales channel.

Approximately 84% of our revenue in 2017 was derived from sales of consumer cardio products. While we continue to be a leader in the consumer strength product category, we believe the much larger market for cardio products offers us greater opportunity for growth.

BUSINESS SEGMENTS AND GEOGRAPHIC INFORMATION

We conduct our business in two segments, Direct and Retail. For further information regarding our segments and geographic information, see Note 20, *Segment and Enterprise-Wide Information*, to our consolidated financial statements in Part II, Item 8 of this report.

SALES AND MARKETING

Direct

In our Direct business, we market and sell our products, principally Bowflex® cardio and strength products, directly to consumers. While we are, and plan to continue to be, a large direct marketer of strength products in the U.S., our advertising emphasis has shifted toward cardio products, especially the Max Trainer® and HVT®, as cardio products represent the largest component of the fitness equipment market and a majority of our business. Sales of cardio products represented 90% of our Direct channel revenues in 2017, compared to 93% in each of the two years 2016 and 2015, respectively.

Our marketing efforts are based on an integrated combination of media and direct consumer contact. In addition to television advertising, which ranges in length from 30 seconds to as long as three minutes, we utilize Internet advertising, product websites, inquiry-response mailings, catalogs and inbound/outbound call centers. Marketing and media effectiveness is measured continuously based on sales inquiries generated, cost-per-lead, conversion rates, return on investment and other performance

Table of Contents

metrics and we strive to optimize the efficiency of our marketing and media expenditures based on this data. Almost all of our Direct customer orders are received either on our Internet websites or through company-owned and third-party call centers.

In order to facilitate consumer sales, we partner with several third-party credit providers. Credit approval rates are an important variable in the number of Direct products we sell in a given period. Combined consumer credit approvals by our primary and secondary U.S. third-party financing providers increased to 54% in 2017 from 51% in 2016 and 48% in 2015. The year-over-year boost in approval rates for 2017 compared to 2016, and 2016 compared to 2015, was due to expansion of credit approval standards, primarily by our Tier 1 third-party credit provider. We believe our marketing and media strategy, which has attracted customers with higher credit scores, has also contributed to the increase in approval rates.

Retail

In our Retail business, we market and sell a comprehensive line of consumer fitness equipment under the Nautilus®, Octane Fitness®, Schwinn®, Universal® and Bowflex® brands. Our products are marketed through a network of retail companies, consisting of sporting goods stores, Internet retailers, large-format and warehouse stores, smaller specialty retailers, independent bike dealers, and to specialty commercial customers purchasing our products for multi-user environments.

We offer programs that provide price discounts to our Retail customers for ordering container-sized shipments or placing orders early enough in the season to allow for more efficient manufacturing by our Asian suppliers. These programs are designed to reduce our shipping and handling costs, with much of the savings being passed on to our customers. In addition, we often offer other types of sales incentives to our Retail customers, including volume discounts and various forms of rebates or allowances, which generally are intended to increase product exposure and availability for consumers, reduce transportation costs, and encourage marketing and promotion of our brands or specific products.

PRODUCT DESIGN AND INNOVATION

Innovation is a vital part of our business, and we continue to expand and diversify our product offerings by leveraging our research and development capabilities. We constantly search for new technologies and innovations that will help us grow our business, either through higher sales or increased production efficiencies. To accomplish this objective, we seek out ideas and concepts both within our company and from outside inventors.

We rely on financial and engineering models to assist us in assessing the potential operational and economic impacts of adopting new technologies and innovations. If we determine that a third-party technology or innovation concept meets certain technical and financial criteria, we may enter into a licensing arrangement to utilize the technology or, in certain circumstances, purchase the technology for our own use. Our product design and engineering teams also invest considerable effort to improve product design and quality. As a consumer-driven company, we invest from time-to-time in qualitative and quantitative consumer research to help us assess new product concepts, optimal features and anticipated consumer adoption.

Our research and development expenses were \$15.4 million, \$13.9 million and \$9.9 million in 2017, 2016 and 2015, respectively, as we increased our investment in new product development resources and capabilities. We expect our research and development expenses to increase in 2018 as we continue to supplement our investment in new product development, technology initiatives, and engineering capabilities.

SEASONALITY

We expect our revenue 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. This seasonality can have a significant effect on our inventory levels, working capital needs and resource utilization.

MERCHANDISE SOURCING

All of our products are produced by third-party manufacturers, and, in 2017, our manufacturing partners were primarily located in Asia. Although multiple factories bid on and are able to produce most of our products, we typically select one factory to be the primary supplier of any given product. Lead times for inventory purchases from our Asian suppliers, from order placement to receipt of goods, generally range from approximately two to three months, of which transit time represents three-to-four weeks. The length of our lead times requires us to place advance manufacturing orders based on management forecasts of future demand for our products. We attempt to compensate for our long replenishment lead times by maintaining adequate levels of inventory at our warehousing facilities.

Table of Contents

We monitor our suppliers' ability to meet our product needs and we participate in quality assurance activities to reinforce adherence to our quality standards. Our third-party manufacturing contracts are generally of annual or shorter duration, or manufactured products are sourced on the basis of individual purchase orders. Our manufacturing relationships are non-exclusive, and we are permitted to procure our products from other sources at our discretion. None of our manufacturing contracts include production volume or purchase commitments on the part of either party. Our third-party manufacturers are responsible for the sourcing of raw materials and producing parts and finished products to our specifications.

LOGISTICS

Our warehousing and distribution facilities are located in Oregon and Ohio. In addition to Company-operated distribution centers, we utilize third-party warehouses and logistics providers to fulfill orders.

In our Direct business we strive to maintain inventory levels that will allow us to ship our products shortly after receiving a customer's order. We use common carriers for substantially all of our merchandise shipments to Direct customers.

In our Retail business we manage our inventory levels to accommodate anticipated seasonal changes in demand. Generally, we maintain higher inventory levels at the end of the third and fourth quarters to satisfy relatively higher consumer demand in the fourth and first quarters of each year. Many of our Retail customers place orders well in advance of peak periods of consumer demand to ensure an adequate supply for the anticipated selling season.

In 2017, approximately 58% of our Retail customers' orders were shipped by our contract manufacturers in Asia directly to our Retail customers locations, typically in container loads. The use of such direct shipments allows us to maintain lower levels of inventory in our warehouses, resulting in lower storage, handling, freight, insurance and other costs, with much of the savings being passed on to our customers. We use various commercial truck lines for our merchandise shipments to Retail customers.

COMPETITION

The markets for all of our products are highly competitive. We believe the principal competitive factors affecting our business are quality, brand recognition, innovation and pricing. We believe we are well positioned to compete in markets in which we can take advantage of our strong brand names, and that our focus on innovative product design, quality, and performance distinguishes our products from the competition.

Our products compete directly with those offered by a large number of companies that market consumer fitness equipment and fitness programs. As the use of Internet websites for product sales by traditional retailers has increased, our competitors have become increasingly similar across our Direct and Retail sales channels.

Our principal competitors include: ICON Health & Fitness, Johnson Health Tech, Peloton, Beach Body, American Telecast, Life Fitness, and Precor. We also compete with marketers of mobile device applications focused on fitness training and coaching on both iOS® and Android™ platforms, such as Workout: Gym exercise planner and NIKE® Training Club. Additional marketers of competitive products include the following: activity trackers and content-driven physical activity products, such as Garmin vivofit® and Fitbit®; computer-based recreation products, such as the Microsoft Xbox®; weight management companies, such as Weight Watchers; group fitness, such as cross-fit classes; and gym memberships, each of which offers alternative solutions for a fit and healthy lifestyle.

EMPLOYEES

As of February 28, 2018, we had approximately 491 employees, substantially all of whom were full-time. None of our employees are subject to collective bargaining agreements. We have not experienced a material interruption of our operations due to labor disputes.

INTELLECTUAL PROPERTY

Trademarks, patents and other forms of intellectual property are vital to the success of our business and are an essential factor in maintaining our competitive position in the health and fitness industry.

Table of Contents

Trademarks

We own many trademarks, including Nautilus®, Bowflex®, Max Trainer®, TreadClimber®, HVT®, Power Rod®, Bowflex Revolution®, SelectTech®, Octane Fitness®, LateralX®, xRide®, Zero Runner®, AirDyne®, and Universal®. Nautilus is the exclusive licensee under the Schwinn® mark for indoor fitness products. We believe that having distinctive trademarks that are readily identifiable by consumers is an important factor in creating a market for our products, maintaining a strong company identity and developing brand loyalty among our customers. In addition, we have granted licenses to a third party to use the Nautilus, Schwinn and TreadClimber trademarks on commercial fitness products, for which we receive royalty income and expanded consumer awareness of our brands.

Each federally registered trademark is renewable indefinitely if the trademark is still in use at the time of renewal.

Patents and Designs

Building our intellectual property portfolio is an important factor in maintaining our competitive position in the health and fitness equipment industry. We have followed a policy of filing applications for U.S. and non-U.S. patents on utility and design inventions that we deem valuable to our business.

We own or license patents and design registrations covering a variety of technologies, some of which are utilized in our selectorized dumbbells, treadmills, exercise bikes, and elliptical machines. Patent and design protection for these technologies, which are utilized in products sold in both the Direct and Retail segments, extends as far as 2034.

We maintain a portfolio of patents related to our TreadClimber® specialized cardio machines, which are sold primarily in our Direct segment. The portfolio includes approximately 23 issued U.S. patents. U.S. patents covering elements of our TreadClimber® products have expiration dates ranging from 2021 to 2027. Expiration or invalidity of patents within our TreadClimber® portfolio could trigger the introduction of similar products by our competitors. Although we view each of the patents within our portfolio as valuable, we do not view any single patent as critical to our success or ability to differentiate our TreadClimber® products from similar products that may be introduced by competitors in the future. We regularly monitor commercial activity in our industry to guard against potential infringement. We protect our proprietary rights and take prompt, reasonable actions to prevent counterfeit products and other infringement on our intellectual property.

We maintain a portfolio of patents and patent applications related to our MaxTrainer® specialized cardio machines, which are sold primarily in our Direct segment. The portfolio includes issued patents with expiration dates ranging from 2024 to 2034, and additional pending patent applications.

Nautilus is also the licensee of patents related to the Bowflex Revolution® home gyms. These patents have expiration dates ranging from 2018 to 2025. Through its Octane Fitness subsidiary, Nautilus owns and licenses certain patents related to Octane's LateralX®, xRide® and Zero Runner® products. These patents have expiration dates ranging from 2018 to 2034.

BACKLOG

We define our customer order backlog to include firm orders for future shipment to our Retail customers, as well as unfulfilled consumer orders within the Direct segment.

Backlog as of a given date fluctuates based on specific timing of product shipment within the typical shipment timeframes for each of our segments. Retail orders comprise the larger portion of our order backlog, while Direct orders comprise a smaller portion of our backlog due to shorter fulfillment timeframes.

Our customer order backlog as of December 31, 2017 and 2016 was approximately \$6.0 million and \$4.9 million, respectively.

SIGNIFICANT CUSTOMERS

In 2017, 2016 and 2015, Amazon.com accounted for 11.9%, 11.3% and 11.1%, respectively, of our net sales.

5

Table of Contents

ENVIRONMENTAL AND OTHER REGULATORY MATTERS

Our operations are subject to various laws and regulations both domestically and abroad. In the U.S., federal, state and local regulations impose standards on our workplace and our relationship with the environment. For example, the U.S. Environmental Protection Agency, Occupational Safety and Health Administration and other federal agencies have the authority to promulgate regulations that may impact our operations. In particular, we are subject to legislation placing restrictions on our generation, emission, treatment, storage and disposal of materials, substances and wastes. Such legislation includes: the Toxic Substances Control Act; the Resource Conservation and Recovery Act; the Clean Air Act; the Clean Water Act; the Safe Drinking Water Act; and the Comprehensive Environmental Response and the Compensation and Liability Act (also known as Superfund). We are also subject to the requirements of the Consumer Product Safety Commission and the Federal Trade Commission, in addition to regulations concerning employee health and safety matters.

Our operations and certain disposed components of our former Commercial business expose us to claims related to environmental matters. Although compliance with federal, state, local and international environmental legislation has not had a material adverse effect on our financial condition or results of operations or cash flows in the past, there can be no assurance that material costs or liabilities will not be incurred in connection with such environmental matters in the future.

AVAILABLE INFORMATION

Our common stock is listed on the New York Stock Exchange and trades under the symbol "NLS." Our principal executive offices are located at 17750 SE 6th Way, Vancouver, Washington 98683, and our telephone number is (360) 859-2900. The Internet address of our corporate website is <http://www.nautilusinc.com>. We maintain an investor relations page on our corporate website accessible at <http://www.nautilusinc.com/investors>.

We file annual reports, quarterly reports, current reports, proxy statements and other information with the Securities and Exchange Commission (the "SEC") under the Securities Exchange Act of 1934, as amended. You can inspect and obtain a copy of our reports, proxy statements and other information filed with the SEC at the offices of the SEC's Public Reference Room at 100 F Street N.E., Washington, D.C. 20549, on official business days during the hours of 10 a.m. to 3 p.m. EST. Please call the SEC at 1-800-SEC-0330 for further information on the Public Reference Room. The SEC maintains an Internet website at <http://www.sec.gov> where you can access copies of most of our SEC filings.

We make our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports, and other information as filed with the SEC, available free of charge on the investor relations page of our corporate website. In addition to our SEC filings, we also webcast our earnings calls and certain events we participate in with members of the investment community on our investor relations page. Further, we use our investor relations page to make presentations and other materials regarding our business and financial performance available, along with our Code of Business Conduct and Ethics, corporate governance policies, and the charters of our Audit Committee, Compensation Committee and Nominating and Corporate Governance Committee. The contents of our websites are not incorporated by reference into this Annual Report on Form 10-K or in any other report or document we file with the SEC, and any references to our websites are intended to be inactive textual references only.

Item 1A. Risk Factors

Nautilus operates in an environment that involves a number of risks and uncertainties. The risks and uncertainties described in this Annual Report on 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 in this Annual Report on Form 10-K actually occur, our business, operating results and financial position could be adversely affected.

Our revenues and profitability can fluctuate from period to period and are often difficult to predict due to factors beyond our control.

Our results of operations in any particular period may not be indicative of results to be expected in future periods, and have historically been, and are expected to continue to be, subject to periodic fluctuations arising from a number of factors, including:

- Introduction and market acceptance of new products and sales trends affecting specific existing products;
- Variations in product selling prices and costs and the mix of products sold;
- Size and timing of Retail customer orders, which, in turn, often depend upon the success of our customers' businesses or specific products;
- Changes in the market conditions for consumer fitness equipment;

Table of Contents

Changes in macroeconomic factors;
Availability of consumer credit;
Timing and availability of products coming from our offshore contract manufacturing suppliers;
Seasonality of markets, which vary from quarter-to-quarter and are influenced by outside factors such as overall consumer confidence and the availability and cost of television advertising time;
Effectiveness of our media and advertising programs;
Customer consolidation in our Retail segment, or the bankruptcy of any of our larger Retail customers;
Restructuring charges;
Goodwill and other intangible asset impairment charges; and
Legal and contract settlement charges.

These trends and factors could adversely affect our business, operating results, financial position and cash flows in any particular period.

The loss of one or more of our large Retail customers could negatively impact our revenue and operating results.

We derive a significant portion of our revenue from a small number of Retail customers. A Retail customer or any of our retail partners may in the future experience difficulties in their businesses that could prompt store closures or reorganizations. A loss of business from one or more of these large customers, if not replaced with new business, could negatively affect our operating results and cash flows.

A decline in sales of Max Trainer® products without a corresponding increase in sales of other products would negatively affect our future revenues and operating results.

Sales of cardio products, especially Max Trainer® products, represent a substantial portion of our Direct segment revenues. Our products are sold in highly competitive markets with limited barriers to entry. Introduction by competitors of comparable products at lower price-points, a maturing product lifecycle or other factors could result in a decline in our revenues derived from this product line. A significant decline in our revenue from this product line would have a material adverse effect on our operating results, financial position and cash flows.

Portions of our operating expenses and costs of goods sold are relatively fixed, and we may have limited ability to reduce expenses sufficiently in response to any revenue shortfalls.

Many of our operating expenses are relatively fixed. We may not be able to adjust our operating expenses or other costs sufficiently to adequately respond to any revenue shortfalls. If we are unable to reduce operating expenses or other costs quickly in response to any declines in revenue, it would negatively impact our operating results, financial condition and cash flows.

If we are unable to anticipate consumer preferences or to effectively develop, market and sell future products, our future revenues and operating results could be adversely affected.

Our future success depends on our ability to effectively develop, market and sell new products that respond to new and evolving consumer preferences. Accordingly, our revenues and operating results may be adversely affected if we are unable to develop or acquire rights to new products that satisfy consumer preferences. In addition, any new products that we market may not generate sufficient revenues to recoup their acquisition, development, production, marketing, selling and other costs.

Currency exchange rate fluctuations could result in higher costs, reduced margins or decreased international sales.

Substantially all of our products are manufactured outside of the U.S. and, therefore, currency exchange rate fluctuations could result in higher costs for our products, or could disrupt the business of independent manufacturers that produce our products, by making their purchases of raw materials more expensive and more difficult to finance. Our future financial results could be significantly affected by the value of the U.S. dollar in relation to the foreign currencies in which we, our customers or our suppliers conduct business. Past fluctuations in currency exchange rates versus the U.S. dollar have caused our costs for certain products to increase, reducing our margins and cash flows. Similar fluctuations and cost increases may occur in the future. If we are unable to increase our selling prices to offset such cost increases, or if such increases have a negative impact on sales of our products, our revenues and margins would be reduced and our operating results and cash flows would be negatively impacted. In addition, a portion of our revenue is derived from sales outside the U.S., primarily in Canada and Europe. Currency rate fluctuations could make our products more expensive for foreign consumers and reduce our revenue, which would negatively affect our operating results and cash flows.

Table of Contents

Future impairments of intangible assets could negatively impact our operating results.

As of December 31, 2017, we had goodwill of \$62.0 million and other intangible assets of \$57.7 million, net of an \$8.8 million impairment charge related to the Octane Fitness brand name. Any future impairment charges, if significant, could materially and adversely affect our operating results. An unexpected decline in revenue, changes in market conditions, changes in competitive products or technologies or a change in management's intentions regarding utilization of intangible assets could lead to future impairment charges.

We are subject to warranty claims for our products, which could result in unexpected expense.

Many of our products carry warranties for defects in quality and workmanship. We may experience significant expense as the result of product quality issues, product recalls or product liability claims which may have a material adverse effect on our business. We maintain a warranty reserve for estimated future warranty claims. However, the actual costs of servicing future warranty claims may exceed the reserve and have a material adverse effect on our results of operations, financial condition and cash flows.

Decline in consumer spending would likely negatively affect our product revenues and earnings.

Success of each of our products depends substantially on the amount of discretionary funds available to our customers. Global credit and financial markets have experienced extreme disruptions in the recent past, including severely diminished liquidity and credit availability, declines in consumer confidence, declines in economic growth, increases in unemployment rates and uncertainty about economic stability. There can be no assurance that similar disruptions will not occur in the future. Deterioration in general economic conditions may depress consumer spending, especially spending for discretionary consumer products such as ours. Poor economic conditions could in turn lead to substantial decreases in our net sales or have a material adverse effect on our operating results, financial position and cash flows.

Our business is affected by seasonality which results in fluctuations in our operating results.

We experience fluctuations in aggregate sales volume during the year. Sales are typically strongest in the first and fourth quarters, followed by the third quarter, and are generally weakest in the second quarter. However, the mix of product sales may vary considerably from time to time as a result of changes in seasonal and geographic demand for particular types of fitness equipment. In addition, our customers may cancel orders, change delivery schedules or change the mix of p