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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the BRP Inc.'s Q3 FY 2019 Earnings Conference Call. I would now like to turn the meeting over to Mr. Philippe Deschênes. Please go ahead, Mr. Deschênes.

Philippe Deschênes - BRP Inc. - Manager of Treasury & IR

Thank you, Maud. Good morning, and welcome to BRP's third quarter conference call for fiscal 2019. Joining me on the call this morning are José Boisjoli, President and Chief Executive Officer; and Sebastien Martel, Chief Financial Officer.

Before we move to the prepared remarks, I would like to remind everyone that certain forward-looking statements will be made during the call that are subject to a number of risks and uncertainties. I invite you to read BRP's MD&A for a listing of these. Also during the call, reference will be made to supporting slides, and you can find the presentation on our website at brp.com under the Investor Relations section.

So with that, I'll turn the call over to José.

José Boisjoli - BRP Inc. - President, CEO & Director

Thank you, Philippe. Good morning, everyone, and thank you for joining us. I am pleased to report that we carried our excellent momentum into this quarter as we continued generating strong retail growth around the world and delivered another quarter of solid financial performance.

The last few months were also marked by good progress on key initiatives to sustain our growth trajectory in the future, such as the successful launch of key product, notably the Can-Am Ryker and the new side-by-side models at our annual dealer event; the positive progress on our different manufacturing capacity increase initiatives in order to meet the growing demand for our products; the integration of Alumacraft and Manitou, the 2 boat companies we acquired earlier this year; and the listing in the United States on NASDAQ. We are very pleased with our overall Q3 performance,

especially considering it is lapping a very strong fiscal year '18 third quarter, fueled largely by the momentum in the side-by-side market that is continuing.

On the back of the solid result we achieved so far this year and the good visibility we have on the remaining months of the year, we are comfortable increasing the lower end of our guidance for the end of the year, bringing our normalized EPS guidance to a range of \$2.96 to \$3.06, representing a growth of 30% to 35% versus last year.

Now let's turn to the financial highlights on the quarter on Slide 4. Our revenues reached a record level for third quarter at \$1,394,000,000, representing a 14% growth over last year's third quarter, primarily driven by the continued strong demand for our side-by-side lineup. Our normalized EBITDA grew 7% and reached \$203 million, and our normalized earnings per share was up 5% to \$1.04.

Our retail sales continued to show robust growth. In North America, our Powersports product retail grew 6% in an industry that was down low single digit in the quarter. Excluding snowmobile, we grew 16% compared to an industry that was up low single digits. As you can see from this slide, our strong growth continued to be driven by the popularity of our Can-Am offroad product lines, where side-by-side is up in the mid-20% range whereas the sector is only up mid-single digit.

ATV sales are up low single-digit percentage, and the sector elsewhere is declining. For our Sea-Doo lineup, we have also performed extremely well. We are up in the high 20% range in an industry that is showing low-teen percentage growth. We are very happy with our Powersports retail performance.

Despite some economic weakness in certain regions of the world, such as the Middle East and parts of Latin America, our product portfolio continued to experience strong consumer demand around the world, driving retail growth of 11% in Latin America, 3% in EMEA and 14% in Asia Pacific.

In EMEA, the stronger industry growth was due to the motorcycle segment in which we don't participate. We have strong retail demand for our product in all key regions. As you can see on this slide, our retail performance has been exceptional since fiscal year '17. Our strategy is paying off, as we continue to push technology and innovation to create market-shaping products.

We have deployed the best value proposition for our dealers, improving their profitability, and they are now more than ever great ambassadors of the BRP brand. With the focus and the solid execution of our team on all fronts, we have been able to outperform our competition and slightly and significantly grow our business.

In September, we held our annual Can-Am and Sea-Doo Club at which we introduced our new product, notably the Can-Am Ryker.

Over the last 2 years, we have put in place teams on the ground in key U.S. states to better understand how we could unlock the full potential of the 3-wheel vehicle category. Two elements emerged that had to be overcome: facilitate the accessibility to the 3-wheel license and address the pricing.

At Club, we unveiled our plan in 3 aspects. First, the introduction of more affordable product. The new Ryker vehicle with an MSRP starting at USD 8,499. It's about 50% lower than the existing entry-level Spyder F3, increasing our addressable market by 2.8x.

Second, to address the price point issue. We repriced the F3 and RT models, and we are offering in the U.S. a leasing option for all our 3-wheel vehicle models. You can now ride a Ryker for as low as \$100 -- \$149 a month.

And third, to provide access to a rider education program. By the end of this year, we will have opened up over 150 schools and have over 9,000 people who have registered to a course, of which 6,500 have already completed it. The rider education program is working and is ramping up.

With this plan in place, we are well positioned to unlock the full potential of the 3-wheel vehicle business. Overall, we were extremely pleased with the reception to the introduction of the Ryker after the dealer event in September. Media tour were conducted in North America and Europe, and we attended some key trade show, particularly in France and Germany, where the reaction was overwhelmingly positive.



So far, we have been very happy with the way the media consumer and dealer have responded and the excellent attention this product has already earned. The media outreach generated over 415 million impressions in just 2 months, outpacing the Sea-Doo Spark benchmark launch in a shorter period. To date, approximately 90% of our dealer worldwide have purchased the Ryker Design Lab, which is a requirement in order to carry the Ryker line. The product is on plan -- the production is on plan, and delivery started this past Monday.

Besides the launch of Ryker, the other highlights of the club included the launch of the seventh new side-by-side platform, the Maverick Sport MAX, which was well received. We also continued to introduce specialized side-by-side like the entry-level Maverick Sport X rc and Defender MAX X mr.

On the Sea-Doo front, the Fish Pro is the first personal watercraft tailored especially for the fishing market, an important growth opportunity with more than 700 million anglers involved in recreational fishing worldwide. Also, we're pleased by the reaction to the waterproof radio we launched in Denver. I would like to remind you that it can be retrofitted to more than 120,000 sparks sold worldwide since 2014.

Now let's turn to Slide 11 for the Year-Round Product highlight. Revenue were up 21% for the quarter, mainly driven by a higher volume of side-by-side sold. On the retail side, we are now 4 months into the season '19, and the industry is up high single digits. For the same period, Can-Am side-by-side retail was up in the high 20%, gaining market share in both the utility and sport segments.

We continued to experience robust demand for our Can-Am side-by-side lineup, and despite the incremental 30% of capacity we had earlier this year, our production is still lagging demand. Work for the second phase of capacity increase at our Juarez 2 facility is well underway, and hourly capacity increase will start ramping up in H1 next year to be full speed beginning H2. The project is on schedule and budget.

Now turning to ATV. The North American ATV industry is also 4 months into the season '19, and retail is down low single digit. For the same period, Can-Am ATV is up low single digit, notably gaining share in the more profitable high-cc segment. For the last 3 years, we have been outpacing the industry, and we are very happy with this momentum.

Finally, a look at the most recent season for the 3-wheel vehicle business. The North American 3-wheel industry ended its season 2018 on October 31 with retail down high single-digit percentage. Can-Am Spyder retail was down mid-single digit over the same period. Season '18 was a transition year for our 3-wheel vehicle business.

We focused our efforts on deploying the rider education infrastructure, managing our network inventory and successfully launching Ryker. We met our objective on all these initiatives, and we believe the progress we have made has positioned us well for a successful upcoming season.

Turning to Seasonal Products on Slide 12. Seasonal Products revenue were up 3%, primarily driven by a higher volume of personal watercraft sold. In terms of retail, it's still early in the season, although the North American snowmobile industry was down in the high-teen percentage.

Ski-Doo retail was also down in the high-teen percentage, primarily due to the later shipment of spring break presold unit and lower level of noncurrent inventory in our network versus the previous year. Our starting noncurrent inventory was 50% lower this year than last year.

And remember, that Spring certificate unit are a special model on which customers put a deposit during the spring season. We have more demand than anticipated for all our models with our new 900 Turbo Powerpack that resulted in later delivery. The good news is that there is snow in North America already, and dealers are extremely busy preparing sled to be delivered to eager consumer.

In Europe, Ski-Doo and Lynx are off to a good start, with quarterly retail up high single-digit percentage in Scandinavia where we started the year with almost no noncurrent inventory. Retail is up low-20% in Russia, a market that continue to recover at a slower pace.

Turning to personal watercraft. The North American industry ended its Season '18 on September 30 with retail up high single digits. Sea-Doo had another very strong season in North America with retail up mid-teen percentage, allowing the brand to reach its highest market share number in history in the region. The strong performance was driven by a record high sell-through on the new Sea-Doo platform introduced last year.



2018 was not only strong in North America but in all RT market as you can see on Slide 13. When looking at the 12-month period ended on September 30, Sea-Doo retail was up mid-20% in Latin America, up mid-20% -- up mid-teen percentage in EMEA and up in the mid-50% in the Asia Pacific region. The next season is looking promising with good early momentum in counterseasonal market as Sea-Doo quarterly retail is already up on average over 35% in Latin America and Asia Pacific region. We are more than happy with our Sea-Doo business.

Continuing with a quick look at Powersport PAC and OEM engines. Revenue were up 13% in the quarter, driven by the continued growth of our accessory sales, notably side-by-side and personal watercraft. The increased growth of side-by-side and personal watercraft sales is having a secondary effect of improving sales on related accessories, especially with our LinQ system. So far this year, we added 450 new accessories, many of which are LinQ compatible and capable of being installed across our product lineup, and this is creating great momentum.

Now looking at the Marine category, our revenue were up 30% in the quarter, driven by the acquisition of Alumacraft and Manitou, which were partially offset by a lower volume of outboard engines sold.

Looking at retail sales, 4 months into the Season '19, the North American outboard engine industry is up low single digits with Evinrude retail down mid-single digits. Internationally, the outboard results were better this quarter, retailing double-digit percentage, driven mainly by Europe and Australia, New Zealand.

I wanted to take a few moments to also update you on our Marine strategy we've previously presented when we announced the creation of the Marine group. As you remember, our buy, build and transform plan is a mid- to a long-term strategy. Similar to what we have done in Powersport business, we want to bring meaningful innovation to the Marine industry. We are in the early stage but progressing well.

One of our first step is to properly integrate Alumacraft and Manitou, including their people and dealers. We attended dealer meeting for both company this fall. For Alumacraft, the boat booking for the upcoming years is in line with last year, despite having 2 large engine OEMs stopping product supply. For Manitou, the pontoon industry is growing at a fast pace, and our order for the upcoming season are up by about 20%. We are happy with our acquisition of Alumacraft and Manitou and the way they are integrating within BRP.

And with that, I will turn the call over to Sebastien and will return for closing remarks.

Sebastien Martel - BRP Inc. - CFO

Thank you, José, and good morning, everyone. As José mentioned, we posted strong results this quarter. And since the beginning of the year, our results are also solid, which is a reflection of our excellent business fundamentals. With year-to-date revenue growth of 16%, normalized EBITDA growth of 27%, normalized EPS growth of 44% and with the continued robust consumer demand for our products, we are in good position to deliver our guidance for the year.

Looking at the quarterly results, revenues were up 14% to reach \$1,394,000,000. The growth was primarily driven by higher volume of side-by-side sold. Revenues grew across all regions, with U.S. being up 19%, Canada up 9% and international up 8%.

We generated \$357 million of gross profit, representing a gross profit margin of 25.6%, down 50 basis points from last year's third quarter, primarily due to unfavorable product mix, which was partly offset by a higher volume of side-by-side and PAC sold.

Our normalized EBITDA was up 7% to reach \$203 million, and our normalized earnings per share was up 5% to reach \$1.04. We generated \$98 million of free cash flow and invested \$79 million of CapEx. We also completed the Manitou acquisition in the quarter for a total consideration of \$75 million.

Turning to Slide 18, our normalized net income was almost flat compared to last year's third quarter due to the following: a net favorable impact from volume, mix, pricing and sales programs for \$41 million and a favorable foreign exchange rate impact of \$4 million, which were offset by higher production, operating and depreciation expense for \$38 million and a higher financing costs and normalized income tax expense of \$8 million.



Now moving to network inventory on Slide 19. Our network inventory is up 9% over last year's third quarter level, primarily driven by higher side-by-side inventory as we are now benefiting from the first phase of capacity increase at our Juarez 2 facility, allowing us to increase shipment cadence and work on catching up with consumer demand for our products.

The growth was also driven by higher PWC inventory, in line with the growing demand for our lineup. Partly offsetting these elements was a reduction in snowmobile network inventory, as we are starting the season with a clean network inventory position.

Finally, turning to Slide 20 for an update on our fiscal year '19 guidance. As I mentioned earlier, given our strong financial results so far this year and with the continued robust consumer demand for our products, we are confident in our ability to deliver our guidance for the year. We have adjusted our revenue guidance upward coming from favorable exchange rates. We are, therefore, planning revenue growth of 13% to 17% and normalized EBITDA growth of 20% to 22%. We have tightened the normalized tax rate to a range of 26.5% to 27% for the year, which is bringing our expected normalized EPS range at \$2.96 to \$3.06, resulting in a growth of 30% to 35%.

Looking at next year, as we mentioned last quarter, given our strong momentum, our objective is to deliver at least \$3.50 of normalized EPS 1 year earlier than initially planned in our 2020 objective. While we have seen the recent implementation of new tariffs over the last 2 months, our objective remains unchanged given the continued strong demand for our products around the world, the very positive reaction to our newly introduced products, the Phase 2 of capacity increase at Juarez 2 that is on plan and is expected to deliver an additional 50% of side-by-side production capacity and our unparalleled innovation capabilities that are providing us with a solid pipeline of product introductions for next year. We are well positioned to continue delivering strong growth.

And with this, I will turn the call back to José.

José Boisjoli - BRP Inc. - President, CEO & Director

Thank you, Sebastien. Overall, we are very happy with our Q3 results, given that we were lapping a strong performance year-over-year for our fiscal year '18 Q3 results. All our product line in the Powersport category are outpacing the competition. Our dealer network and the media welcomed our new product with keen interest, and we expect our consumers to feel the same way.

Our Marine strategy has progressed with the acquisition of 2 boat companies and, over the mid- to long term, will lead us into new opportunities. The team around the world is executing very well, and I'm proud of their contribution.

Despite some headwinds in a still volatile environment, we are executing on our plan, and we continue to outpace the industry. I strongly believe that the strength of our diversified product portfolio, our global distribution capabilities and our world-class manufacturing footprint is what has made us successful and what differentiates us from the competition.

As mentioned, we are well positioned to deliver a record year with normalized EPS growth of 30% to 35%. And we are confident we'll be able to deliver at least \$3.50 EPS for fiscal year '20 in the current economic's context. Our product lineup have never been as strong with our diversified product portfolio, and the engagement from all our dealers is high. The fundamentals of our business are very strong, and we are excited with our momentum.

On that, I will turn the call over to the operator for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question is from Gerrick Johnson from BMO Capital Markets.

Gerrick Luke Johnson - *BMO Capital Markets Equity Research - Senior Toys and Leisure Analyst*

My first round will be focused on boats here. Thanks for the purchase price on Triton, but can you talk about the annual sales run rate for Triton, Manitou? And also what the boat contribution was in the quarter? And perhaps how the integration is going at the dealer level? I guess that's good for now, and I'll follow up later.

José Boisjoli - *BRP Inc. - President, CEO & Director*

Gerrick, I will take the dealer question, and Sebastien will take it from there. Just to give you a sense, it's just starting. Obviously, there was some other OEM brand, engine OEM brand, that decided not to continue with Alumacraft. But I think it's too early to give feedback, but we feel comfortable. On the Alumacraft side, we've lost maybe 20 dealers so far. But we have 50 Evinrude dealers that raised their hand to take over the brand, then we feel comfortable. And I would like to remind you some numbers: Alumacraft has about 275 dealers, mainly east of North America; Manitou, 150 in the Midwest; and Evinrude, we have a 1,000 dealers coast-to-coast. Then we -- there is maybe some short-term disruption in the dealer network because some other engine brand need to decide if they will continue to carry Alumacraft and Manitou. But midterm, we don't see any problem going forward. Sebastien?

Sebastien Martel - *BRP Inc. - CFO*

On the revenue numbers for the quarter, the boat acquisitions had less than 3% of the quarterly revenue. And when I look out for next year, it should be about that 3%. So we're looking at about probably \$200 million of revenue from the boat businesses then, Gerrick.

Operator

Our following question is from Robin Farley from UBS.

Robin Margaret Farley - *UBS Investment Bank, Research Division - MD and Research Analyst*

Great. I wonder if you could give some color around average selling price on the offered in the side-by-side business and just kind of a little more color on what's happening with margin there just with your revenue guidance raise but not your EBITDA guidance raise.

Sebastien Martel - *BRP Inc. - CFO*

Yes. When I look at ASPs for the quarter, I'll give it more broadly, ASP was flat for the quarter. And I alluded to mix being unfavorable this quarter. And so that brought the ASP down for side-by-sides. If you'll recall, last year, we introduced the Maverick Sport, the Trail and now we have a 60-inch Maverick Sport. And so we'll obviously, in year 2 of product announcement, we're shipping more of those products to dealers. And so that's what impacted ASPs this quarter. And on the ORV side, mix was reached and the ASP was up. But overall, Robin, flat ASP all product lines on the Powersport side (inaudible).

Robin Margaret Farley - *UBS Investment Bank, Research Division - MD and Research Analyst*

Great. And just kind of thinking about margins with the increase in revenue guidance but not EBITDA, just can you talk us through a little bit about that dynamic?

Sebastien Martel - BRP Inc. - CFO

Yes. Well, we've been seeing favorable exchange rates in the last few months. And so in Q3 as well, the rates were favorable. The rates are turning above \$1.30 for the U.S. And as you know, we are kind of naturally hedged throughout the year, our bill of material cost versus our expenses and our revenue. And so yes, we're seeing a revenue uplift. But because of the hedging position that we have, we're not seeing that flow down to the bottom line. And so the drive and 100% of the adjustment in revenue comes from (inaudible).

Operator

Our following question is from Mark Petrie from CIBC.

Mark Robert Petrie - CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research & Research Analyst

I want to ask about Ryker. Obviously, good response from the dealers. But just in terms of magnitude, how was the takeup on sort of Ryker and the Design Lab compared to how dealers have been positioned with Spyder? And I guess sort of related to that, what's your sense of how dealers are allocating space within their dealership? I mean, are they giving up floorspace from Spyder to Ryker? Or sort of how is that kind of playing out at this point?

José Boisjoli - BRP Inc. - President, CEO & Director

Yes. Mark, first, we are -- in North America, we are exactly on plan in terms of the number of Ryker we booked. At international, the demand is about 25% higher than what we had originally planned, but those shipments will happen next year. Now it's a very good question because we believe that the Design Lab is critical for the experience for the consumer. As you know, we have only 3 SKUs, and the customer can customize on-site the Ryker. And that's why the dealers need to buy the Design Lab to carry Ryker. And so far, we're happy. In Europe, almost every dealer have purchased the Design Lab. And in North America, about 90%, and some decided not to continue with the Spyder business because it was too expensive. Then we've lost probably 40, 50 dealers in North America. But on the other hand, many dealers who were not carrying Spyder have raised their hand. But so far, we're very, very happy with the booking, with the take rate on the Design Lab. And also the first feeling we have from the media and the press is very, very positive. And as I mentioned in my intro, we started to deliver the Ryker this Monday. The target is every dealer should get 2 in their store for demo before Christmas.

Mark Robert Petrie - CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research & Research Analyst

Okay. That's helpful. And then I guess, just sort of more of a high-level question, obviously, you've got a lot of capacity coming on next year. You reiterated your EPS target for fiscal 2020, and you remain confident. But at a high level, can you just sort of share your assumptions or, generally, how you're thinking about the macro environment and sort of the health of the consumer and industry demand over the next kind of 12 to 18 months?

José Boisjoli - BRP Inc. - President, CEO & Director

Well, let's say that, obviously, we are not economists. But the interest rate has increased, and many are a bit concerned that it will impact the consumer demand. But to be honest, in Q3, the traffic at the store were good as you can see in our retail. And so far, I mean, in Q3, watercraft and side-by-side were up about 25%. And in Europe, it was the same thing. Then we don't see any impact at the retail level. And like I said, the traffic was still very good. And I would like to say most of our industry are still growing. I think everyone -- everything is growing except ATV, which is flattish, and the snowmobile, which is too early to conclude anything. Then we understand that there is some concern on the global economy, but we don't see that at our level. And we believe that as long as the unemployment rate is low and the housing market is, I would say, okay, we are in good shape.

Operator

Our following question is from Benoit Poirier from Desjardins Capital Markets.

Benoit Poirier - *Desjardins Securities Inc., Research Division - VP and Industrials, Transportation, Aerospace, Industrial Products & Special Situation Analyst*

Could you provide some comments about your inventory at the retail level? More about the age of the inventory? And what type of expectation, what should we expect in terms of inventory going into the fourth quarter and fiscal '20?

Sebastien Martel - *BRP Inc. - CFO*

Yes. Benoit, when I look at the overall inventory position, yes, the inventory is up this quarter, but for the right reasons. Retail, when it excludes snowmobile, is north of 16%; inventory, up 9%. So I'm very comfortable with the inventory that we have. When I look at aging as well, units above 18 months is less than 5% of our -- of the inventory that's outstanding. My outlook for the fourth quarter is that inventory is going to continue to increase coming by 2 elements. One, with side-by-side, I mean, demand is there. We have -- we're still not meeting consumer demand. So obviously, we'll be shipping side-by-sides to the dealers ahead of the spring season that's coming. And also, as José mentioned a few minutes ago, we started shipments of Rykers. And so we'll be busy shipping in December and January. And so I'm expecting side -- not side-by-side, but Spyder inventory will also be up. For snowmobile, there's snow on the ground, so hopefully, we'll have a good season and we finished off with clean inventory last year. So I would expect snowmobile to be relatively flat versus the year ago.

Benoit Poirier - *Desjardins Securities Inc., Research Division - VP and Industrials, Transportation, Aerospace, Industrial Products & Special Situation Analyst*

Okay. That's very good color. And when we look at your recent stock performance, any thoughts about your interest for renewing your NCIB that was completed earlier this year, Sebastien?

Sebastien Martel - *BRP Inc. - CFO*

As you've said, we completed the NCIB in July. The next window is going to open in Q1 of next year, so we've done everything that we could do under the NCIB. But obviously, when we look at where the share price is trading and the valuations, it's part of the discussions we're having with the board in terms of using our capital. Our balance sheet is strong. Our priority #1 is to continue investing in growth. But obviously, we'll be opportunistic if we need to be.

Operator

Our following question is from Derek Dley from Canaccord Genuity.

Derek Dley - *Canaccord Genuity Limited, Research Division - MD & Consumer Products Analyst*

Just a question on the PWC growth, obviously quite strong during the quarter. Can you comment just on the split of that growth between some of your higher-end models versus the Spark?

José Boisjoli - BRP Inc. - President, CEO & Director

Yes. Derek, yes -- I mean, we have more than 50% of the industry, then -- the market share. Then when, I mean, we have success in a segment, we pull the segment up. But basically, the high end, what we call internally the luxury performance, the industry was up this season by about 50%, and we were up by more than 30%, then we really -- that's proved the success of the new platform that we introduced last year. Recreational was up mid-single digit. We're up high single-digits, and Rec Light was flattish at mid-single digit. Then as you can see, every segment is growing, and we're outpacing the industry in luxury performance and recreational line. Overall, we're very happy in this, our numbers from North America, but the phenomena is the same worldwide.

Derek Dley - Canaccord Genuity Limited, Research Division - MD & Consumer Products Analyst

Okay. That's very helpful. And just on the inventory position, Sebastien, I appreciate your comments on the snowmobile side. But can we just talk about some of the other business lines? And is it mostly relatively current inventory that's in the channel right now?

Sebastien Martel - BRP Inc. - CFO

Yes, very current. Again, we finished clean on snowmobile last year, so what we're shipping is current models. Watercraft, we finished a bit higher, but that's in line with overall market performance and market growth. ATV, I mean, we continue gaining market share, so that's clean inventory. And for side-by-side, well, most of it is driven by the new models that we've introduced.

Operator

Our following question is from Craig Kennison from Baird.

Craig R. Kennison - Robert W. Baird & Co. Incorporated, Research Division - Director of Research Operations and Senior Research Analyst

So just to follow up on the inventory question, I apologize if I missed it, but do you have inventory growth excluding the snowmobile category?

Sebastien Martel - BRP Inc. - CFO

I do not have it with me, but I could -- we could rummage around and see before the end of the call if we could pull it out. But or else, we'll be glad to provide that info to you.

Craig R. Kennison - Robert W. Baird & Co. Incorporated, Research Division - Director of Research Operations and Senior Research Analyst

Okay. And then José, how should investors view the turnover in leadership in the Powersport segment? Obviously, you brought in a lot of good talent there, but there's been change.

José Boisjoli - BRP Inc. - President, CEO & Director

Yes. I mean, Bertrand came to the company, it was a new industry for him. He came from the car industry. And after 10 months, he and I felt that the fit was not there, and he wanted to continue with something else. And we've looked at what were our options, and we have, as you know with Sandy Scullion, who've been with the company for more than 20 years, and Thomas Uhr, who was in Austria for 5 years. We have very good, talented persons who will co-lead the Powersports group. Just so you know, Thomas that you met when we were in Austria in 2015 has accepted to move to Canada with his family. Then the minute that we'll get his working permit, he will move here, and both of them will be based here. Then those things happened, but very happy that we have very talented people internally.

Craig R. Kennison - *Robert W. Baird & Co. Incorporated, Research Division - Director of Research Operations and Senior Research Analyst*

And then finally, just getting back to the macro environment, we have seen reports of more farmer bankruptcies in the Upper Midwest of the United States. How would you characterize your exposure to that farm economy? And are you seeing any weakness in trends there? I know you've got Defender, which is gaining a lot of share. So maybe that masks some of the weakness but curious what you're seeing.

José Boisjoli - *BRP Inc. - President, CEO & Director*

Yes. We don't see much. I mean, the all-in ag patch that we call, we don't see much. Those states are still somewhat depressed. And for us, like you just said, it's very difficult to analyze because the Defender momentum is masking the slower industry. That's for United States. Canada is still soft in the West versus the East. But as you can see with the momentum we're gaining with our side-by-side business, all of this is masking those slow growth or flattish state in United States.

Operator

Our following question is from Cameron Doerksen from National Bank Financial.

Cameron Doerksen - *National Bank Financial, Inc., Research Division - Analyst*

I guess just to follow up on the snowmobile retail in the quarter, I just wondered if you could just go over again what's sort of the key driver there, results of the retail softness. I mean, the way you described it, it sounds more of a timing issue than anything. And then also if you could just maybe comment on what you're seeing so far subsequent to quarter end with snowmobile and retail? I mean, you mentioned the early snow in a lot of parts of North America that should bode well, but just wondering what you're seeing so far.

José Boisjoli - *BRP Inc. - President, CEO & Director*

Yes. Obviously, I would like to remind you that we have 50% of the industry. Then when we are -- when the timing of what we're doing is affecting our retail, it's affecting the industry but somewhat -- -- basically, in the noncurrent, we started the year, this year, with 25% of the noncurrent inventory, and our market share is 50% plus then. This is affecting our start of the season. On the other hand, the spring unit, we always have a very high level of snowmobile that are presold to customers. But the popularity of all the model with the 900 Turbo resulted that we're shipping those models a bit later than what was planned originally because the volume was at twice as what we were planning. And then there was another phenomena. I was with the dealer from Milwaukee Wednesday evening, and he was telling me that he wants to raise the sum of his watercraft every year. And the customer, with the warm fall we had, the customer kept the watercraft on the water very long, then he went to rise basically his watercraft about a month later than typically and started to focus on (inaudible) snowmobile at a high speed a month later. Then I think there is all those moving parts that is affecting the retail season. But with the good snow we have here in the East, it's a bit weaker in the west of Canada. But the overall, I would say it's a very good start of the season, and we're not worried with the snowmobile season.

Cameron Doerksen - *National Bank Financial, Inc., Research Division - Analyst*

Okay. That was very good. And maybe just a second question from me, I mean, we've talked a bit about the macro, right, environment. I mean, it doesn't sound like you're seeing any real weakness there at this point. But can you maybe just discuss what your flexibility is to reduce your cost base in the event that we do have a slowdown in demand? I mean, just what kind of flexibility do you have with your manufacturing, I guess, overhead cost to reduce your cost base in that kind of eventuality?

José Boisjoli - BRP Inc. - President, CEO & Director

Yes. That's a good discussion that we had with the board yesterday. Our situation is quite different than what happened in 2008. And just to give you a sense, today, we have a lot more diversified product portfolio. We're less dependent on Seasonal Products than we were before. We entered the side-by-side utility segment with the Defender, which is, we believe, a more stable industry when you have big fluctuation with the economic environment. Our network inventory with the order management system that we have in North America, the dealer order every month, then we believe off-road will be adjusted very quickly down. And we are more diversified today than we were in '08, '09. We did continue to increase our global sales worldwide. Our manufacturing footprint is more flexible. We can move product around between product line. And our debt, lower leverage, covenant-light, then we have a lot more flexibility than what we had in '08. And BRP is a company that had been through many, many cycles, and we can react very quickly if things happen. Then we're not looking for those period, but we believe we are in good shape versus where we were in '08 and '09. And obviously, '08, '09 was a very, very bad recession.

Operator

Our following question is from Jamie Katz from Morningstar.

Jaime M. Katz - Morningstar Inc., Research Division - Equity Analyst

First, I'm interested in hearing about international markets, particularly Western Europe. In the table in your financial statement release, it appears that Western Europe trailed a little bit this quarter. And I'm curious if that is either FX-related or if there's a certain consumer segment that's acting as a lag in that region.

José Boisjoli - BRP Inc. - President, CEO & Director

Yes. Jamie, what happened in Western Europe is 2 phenomena. First, this fall in Q3, the retail for watercrafts was very, very good because it was a very warm fall, and our dealer are almost sold out of watercraft. But it was a bit slower on the off-road business, and we believe it's because the weather was so hot. I mean, when it's 35 Celsius, it's a bit -- it's not comfortable to purchase an [EVR] side-by-side. And the watercraft was good, then traffic was good in the dealership, a bit less in off-road. But the big drive came from the motorcycle business. There was -- it was a good season for motorcycle in the mid-cc segment in a category that we don't participate in any of our product line. Then this is how we see the situation in Western Europe. In Scandinavia, where we are, we're very, very strong with very high level of market share in every product line. The retail was good overall.

Jaime M. Katz - Morningstar Inc., Research Division - Equity Analyst

Okay. And then you commented briefly on tariffs in your prepared remarks, but I'm curious if you have any quantifiable insight into how that maybe has affected the business, given the amount of sales that are completed in the U.S., positive or negative.

Sebastien Martel - BRP Inc. - CFO

Yes. Jamie, last quarter, when we talked about inflationary elements for fiscal year '19, the current fiscal year, versus guidance, I alluded to a \$25 million impact for this year and also talked about impact for next year of about \$25 million as well. What came into effect since we last talked was the Section 301, the List 3 tariffs, which were, I guess, confirmed and communicated. And those tariffs impact mostly our PAC business as we buy goods from China and import them into the U.S. And so what I'm estimating in terms of cost for next coming from those tariffs, the List 3, is about a \$10 million impact for next year. So...



Jaime M. Katz - Morningstar Inc., Research Division - Equity Analyst

Okay. That's actually better.

Sebastien Martel - BRP Inc. - CFO

Pardon?

Jaime M. Katz - Morningstar Inc., Research Division - Equity Analyst

It's actually better than you originally anticipated.

Sebastien Martel - BRP Inc. - CFO

No. Well, actually, I still -- we still have about \$25 million coming from commodities, freights. So that's still there. So the \$25 million is there, so add the extra \$10 million on the \$25 million. So about a \$35 million impact for next year. Again, it's material, but it's obviously something that we can manage. As every year, we do have inflation. And as customary, we have our cost efficiency programs that are in place, and we'll address those cost increases appropriately as well. But yes, despite all of that, we're still comfortable on delivering the \$3.50 for next year.

Operator

(Operator Instructions) Our following question is from Seth Woolf from Northcoast Research.

Seth Woolf - Northcoast Research Partners, LLC - VP & Research Analyst

I guess just talk about the -- I want to talk on off-road vehicles and marine industry. So first of all, in your Year-Round Products, did you get a chance to figure out what the growth was ex snowmobiles? And then I think, José, you said that as the capacity comes online, you're starting to meet consumer demand now. So how should we think about this going into next year? Is this a number in the dealer inventory? Are we going to see that continue to rise and maybe accelerate?

José Boisjoli - BRP Inc. - President, CEO & Director

Well, let's clarify a few things. The capacity increase in Juarez 2 is for side-by-side. We will start to ramp up the speed of the line Feb 1, but it will take about 6 months to reach the 50% increase that we're planning. Then the real -- it will start from low numbers February 1. And by the end of H1, we'll be at 50%. Then next year, our capacity for additional side-by-side will be about 25% more than what we've done this year. And that's probably the simpler way to give you more colors about what we're planning for next year.

Sebastien Martel - BRP Inc. - CFO

Yes. In terms of inventory excluding snowmobile for North America, it would be in line with the retail that we had excluding snowmobile. So we're looking at a high-teen increase in inventory, coming obviously from side-by-side with the retail growth that we have experienced in the quarter and also personal watercraft with the added inventory we finished the season with compared to last year.

Seth Woolf - *Northcoast Research Partners, LLC - VP & Research Analyst*

Okay. And so I'm assuming so your returns are probably coming down because you're catching -- you're filling the channels with what they've been short on? Is that right?

Sebastien Martel - *BRP Inc. - CFO*

Well, the turns obviously are good now because we have trouble meeting consumer demand on side-by-side. And so as we ramp up capacity next year, the terms should reduce a bit. But our objective is to maintain a level of inventory in the range of 120 days to 160 days in the network. So we're always cautious of maintaining those ratios. And we believe that's a healthy level of inventory that the dealers can support and making sure that they have the right products for the consumers.

Seth Woolf - *Northcoast Research Partners, LLC - VP & Research Analyst*

Okay. That's excellent. And then just turning to Marine business, throughout the number for Manitou, 20%, orders are up 20% year-over-year, I think, coming out of the dealer show. Is there anything different that you guys have done from a model standpoint? Or what, it's just the strength of that market is the underlying driver, do you believe?

José Boisjoli - *BRP Inc. - President, CEO & Director*

No. But on Manitou, Evinrude have been always strong. We rigged more -- about 35% of their pontoon already. Then Manitou dealers were used to sell Evinrude. Then, like you said, the pontoon industry is up high, about 15%. Then we were able to -- then it was a good show. Dealer were enthusiastic now that Evinrude and Manitou are together. We're working on a strategy where we will rig from factory more pontoon, then it makes their life easier, and we believe it's all this that created the momentum. Then it's a combination of good industry momentum and the popularity of the Manitou product.

Operator

Our following question is from Gerrick Johnson from BMO Capital Markets.

Gerrick Luke Johnson - *BMO Capital Markets Equity Research - Senior Toys and Leisure Analyst*

Just on gross margin, the gross margin down 50 basis points year-over-year. Can you just please, Sebastien, quantify a basis-point hit or a tailwind or headwind from mix, leverage, inputs and the other components of gross margin?

Sebastien Martel - *BRP Inc. - CFO*

Yes. Mix was a big factor this quarter. I talked about snowmobile, utility sleds that we shipped versus mountain. I also talked about the Maverick Sport. That was a hit of 130 basis points, and that was offset by volume, 80 basis points. So in a nutshell, these 2 elements drove the margin down by 50 basis points in the quarter.

Gerrick Luke Johnson - *BMO Capital Markets Equity Research - Senior Toys and Leisure Analyst*

Okay. So no major swing either way on inputs then?

Sebastien Martel - BRP Inc. - CFO

No. Well, production cost is about 40 basis points negative but was offset by pricing. But again, 40 basis points, considering the environment in which we are, I'm pretty happy with that level of impact. And so the teams were able to react appropriately, and our cost reduction programs are actually paying off.

Gerrick Luke Johnson - BMO Capital Markets Equity Research - Senior Toys and Leisure Analyst

Okay. And then related to that, how about program expenses of percent of growth sales this year versus last year?

Sebastien Martel - BRP Inc. - CFO

Relatively flat. No variance in terms of margin. As you saw, the retail was strong. The pull from the watercraft was excellent. As José alluded to the new platform, the turnover on the new platform was strong, so we didn't necessarily have to put any programs. So year-over-year, flat.

Operator

We have no further questions registered at this time. I would now like to turn the meeting back over to you, Mr. Deschênes.

Philippe Deschênes - BRP Inc. - Manager of Treasury & IR

Thank you, Maud. And thanks, everyone, for joining us this morning, and thanks for your interest in BRP. We look forward to speaking with you again for our year-end conference call in March. Thanks again, and have a good day.

Operator

Thank you. The conference has now ended. Please disconnect your lines at this time, and we thank you for your participation.

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