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# EDITED TRANSCRIPT

ELY - Q4 2012 Callaway Golf Earnings Conference Call

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**OVERVIEW:**

ELY reported full-year 2012 consolidated sales of $832m and 4Q12 sales of $118m. Expects 1H13 sales to be $555m and EPS to be $0.33. Expects 2013 sales to be $850m and diluted loss per share to be $0.04.





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## CORPORATE PARTICIPANTS

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**Andrew Burns** *Davidson - Analyst*

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**Craig Kennison** *Robert W. Baird - Analyst*

## PRESENTATION

**Operator**

Good afternoon my name the Allie and he will be your conference operator today. At this time I would like to welcome everyone to the Callaway Golf fourth quarter 2012 Earnings Conference Call. (Operator Instructions). I would now like to turn the conference over to your host Brad Holiday, Chief Financial Officer. Mr. Holiday, you may begin your conference.

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**Brad Holiday** - *Callaway Golf - CFO*

Thanks, Allie. I would like to welcome everyone to Callaway Golf Company's fourth quarter 2012 Earnings Conference Call. Joining me today is Chip Brewer our President and CEO.

During today's conference call Chip will provide some opening remarks and I will provide an overview of the Company's financial results for the quarter, and we will then open the call for questions.

I would like to point out that any comments made about future performance, events, prospects or circumstances including statements relating to estimated net sales, gross margins, operating expenses, net income and per share results for 2013, the estimated amount or timing of benefits and charges associated with the cost-reduction initiatives, future market recovery, growth opportunities and market share gains, the success of our 2013 product line, the Company's turnaround and the collectibility of our Accounts Receivable, as well as the Company's estimated 2013 capital expenditures, and depreciation and amortization expenses are forward-looking statements subject to Safe Harbor protection under Federal securities laws. Such statements reflect our best judgment today based on current market trends and conditions. Actual results could differ materially from those projected in the forward-looking statements.

As a result of certain risks and uncertainties applicable to the Company and its business. For details concerning these and other risks and uncertainties you should consult our earnings release issued today as well as part 1 Item 1A of our Form 10-K for the year-ended December 31st, 2011 filed with the SEC together with the Company's other reports subsequently filed with the SEC from time-to-time.

In addition, during the call in order to assist interested parties with period-over-period comparisons on a consistent and comparable basis we will provide certain pro forma information as to the Company's performance excluding charges associated with the Company's Global Operations Strategy, non cash tax adjustments including a deferred tax valuation allowance, restructuring charges, the gain on the sale of three buildings, the gain on the sale of Top-Flite and Ben Hogan brands, non cash impairment charges and charges related to the Company's cost-reduction initiatives.

We will also provide information on the Company's earnings excluding interest, taxes, depreciation, amortization expenses, and the non cash impairment charges.

This pro forma information may include non-GAAP financial measures within the meaning of Regulation G. The information provided on the call today and the earnings release we issued today include a reconciliation of such non-GAAP financial measures to the most directly comparable financial measures prepared in accordance with GAAP. The earnings release is available on the Investor Relations section of the Company's website at www.callawaygolf.com.

I would now like to turn call over to Chip.

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

Thanks, Brad. Good afternoon everybody and thanks for calling in this afternoon. I'm glad to be with you today and have the opportunity to discuss our results as well as the many changes happening here at Callaway Golf.

2012 was an interesting and challenging year for Callaway. Although we ended year within our most recent guidance, our financial results were clearly below acceptable levels and for the year as a whole we lost market share in the US, our largest market. Brad will review the 2012 financials with you in a minute.

From a market share basis, through November our US hard goods market share declined to 14.4% versus 15.6% in 2011. That's a decrease of 8%. To say these metrics are disappointing would be an understatement.

Fortunately, I believe the bigger story is the turnaround and transformation that occurred during the year. This transformation paired with the strength of our global brand and recovering market conditions is our primary investment thesis. Internally when we talk about our change effort we talk about a new Callaway. One that builds on its considerable strength and history but is also much more dynamic and contemporary.

I'm proud of the pace and direction of our change efforts and at the risk of being redundant with either the press release or previous comments during other earnings calls I think it would be helpful to review some of our progress and accomplishments of last year. These include successfully stabilizing our market share during the second half of this year, thus, halting a long-term trend of market share losses that we have been experiencing in the US market while gaining market share in key markets such as Korea and Japan and also clearing inventories both at Callaway and in the field.

The refocusing of our business on its core of golf clubs and golf balls. During 2012 we sold Top-Flite and Ben Hogan, licensed apparel and footwear and discontinued direct operations in electronics or GPS business. We rebuilt our senior Management Team via a combination of additions from the outside and changes within. Included within this new leadership is new leaders in Global Operations, legal, product development, marketing and North American sales.

We lowered our cost structure via various cost-reduction initiatives which totalled $60 million in annualized savings. We restructured and improved our sales organizations in both the Americas and Europe. We believe we built a more effective supply chain to improve costs, product development and customer service including bringing in a new senior leadership to run this important department. The Ops team accomplished numerous cost andefficiency improvements spanning from the range of working with vendors to assembly, through logistics.

Two specifics there are the streamlining of the Chicopee operation and improvements in Monterey, our assemblies facility, as we converted that to a cellular and lean operation. When I showed up at Callaway in March of last year our custom fitting delivery was unreliable and thus a liability in the marketplace. This year we expect it to provide a competitive advantage and are promising five day turnaround from order entry into the customers' hands for custom orders in North America.

Tour is an important element for success in the golf industry and we believe we have strengthened our global tour staff to compliment our icons such as Phil and Ernie we have added new youth and bombers on the US PGA tour such as Gary Woodland, Chris Kirk, Luke List, James Hahn, Andres

Gonzales,and Brian Stuard. In the European theater we're building on strength there with additions of European Ryder Cup star Nicolas Colsaerts and also Challenge Tour sensation Kristoffer Broberg who won four times on the Challenge Tour in 2012.

And then last but not least the addition of Rio Ishikawa. Ryo is and incredible celebrity and a source of national pride in Japan who at 21 years of age is on track to becoming an international star. Ryo is a big and bold bet for Callaway Golf but one that fits with our overall global strategy, and has the potential to drive significant growth in a highly profitable market, and also supports what we believe is and exceptionally strong Management Team and an exceptionally strong brand position for Callaway in Japan.

On the marketing side there's been much discussion at Callaway over the last three years. And we have clearly changed both our approach and strategy including bringing in new senior leadership to run this important department. We are finally starting to see some of our 2013 efforts here and I think you have to agree that as promised they are different and in my opinion they are better. The creative is more authentic and benefit-oriented. The messages are more compelling and simpler. For example, the "Longest Driver in Golf" and "Fairway Woods That Are Longer From Everywhere."

Our marketing is often more creative and fun. Two examples here, one, bomb patches. If you checked our website you will be able to see these. It is a concept borrowed from college football where they put stickers on the helmets for great plays.

Our athletes on tour are getting bomb patches for drives over 325 yards and they're already talking about it. The digital space is a-buzz with it and we believe that media will pick up on it. Players such as Tommy Gainey have over 20. Andres Gonzales has appointed himself as the commissioner of the bomb patch lead and is keeping score. And players are competing for the honor of the bomb patch.

On the coverage on TV both cable and network you're going to see the long drive of the day. That is a concept again borrowed from football where when you watch and you see the yellow first down lines that are displayed onto the screen. Each day under the coverage you will see the Callaway X Hot Bomb of the day which is the long drive of that day. And we're hopeful that some of our bombers will be participating in that celebration. We're also much more engaging and active in the digital space thereby creating advocates and early buzz.

In my opinion all of these changes on the marking side are tried and true approaches. We know these work and, thus, as industry veterans we believe we're actually taking risk out of the proposition and yes, it is refreshing and energizing.

Moving to product. This is product is always the keystone of our business. And during 2012 we overhauled our product strategy and execution. Our 2013 products are more contemporary in appearance and aggressive in the performance benefits they deliver.

These products include the Razr Fit Extreme Woods, the X Hot line of woods, hybrids and irons, the Versa putters and the HX Hot golf balls. All of those products are outstanding but there's one I want to go into a little more detail with you not only because of potential but also because of what it says about this team and this company. That product is the X Hot Fairway Woods.

High COR, or spring-like effect Fairway Woods were the story of the year in 2012 and Callaway wasn't part of it. When I arrived in March of last year, we still had no plan to be in the category for 2013 and many thought it was too late to do so. The team here not only did it. They set a new standard. An incredible engineering accomplishment combined technologies we borrowed from our past with some creative new technologies as well as new manufacturing capabilities, the tolerances that we're holding in part of the process for these X Hot Fairway Woods are tighter than those used for the turbines in aerospace.

The result is the hottest stainless Fairway Wood in golf that is still also easy to hit as we say "Longer from Everywhere." You combine this with the contemporary appearance that listened to the market even when it was inconvenient or expensive to do so and I believe we go from not-in-the-game to what I believe is the best Fairway Wood in golf. As an industry veteran and unabashed product guy seeing this reaffirms that I'm at the right place. A place ripe with promise and potential.

As you expect based on the comments made so far the feedback from customers and consumers has been positive. Our 2013 line is being received very well, certainly better than recent years. As usual I invite you to your own channel checks to confirm or refute my point of view on this. However, having said that, I do pride myself in having good relations and communication with customers and thus I believe you will be encouraged by what you find.

As a result of all of the above our expectation is to regain hard goods market share in each of our key regions in 2013. Most importantly, we're making great progress in reenergizing our culture and rebuilding morale. An ongoing change effort which I'm happy it to report is progressing well. People see substantive change and although some of the changes are difficult I believe the vast majority agree with them and are energized by the new direction. When you reflect on all these buzz accomplishments and what's different and combine it with the fact that the US markets appear to be recovering, Europe will undoubtedly recover at some point and the long-term growth opportunities that exist in developing markets there is reason for optimism.

Indeed, I am confident that Callaway Golf is in a much stronger position today and that these changes will show themselves in improved financial performance going forward. However, I also need to emphasize that turnarounds take time. As I have said on previous calls, this will be a multi-year process. There is still much to do, markets will undoubtedly remain hyper-competitive, and we know that the ultimate success will be determined by the consumer as measured by sell-through. And unfortunately it is too early to get a good read on that.

As for 2013 we are providing guidance for revenues of $850 million and break even net income. Given Callaway's performance and trends over the last several years this would be a considerable improvement. Beyond this given the magnitude of the change effort the uncertainties of the market, we are uncomfortable providing further specific guidance beyond 2013 however, we do believe that 2013 is just a start and that this team will deliver further improvement. In closing I remain confident that the clear and specific actions we are taking will in fact turn this business around and that we have a promising long-term outlook. I look forward to continuing to keep you updated on our progress and I appreciate your interest and support.

Brad, over to you.

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**Brad Holiday** - *Callaway Golf - CFO*

Thank you, Chip. As Chip mentioned we made significant progress in restructuring and making changes in the Company over this past year and we are all looking forward to the 2013 season. Let me quickly review our results for the quarter and full year.

Because of the significant charges associated with our costs reduction in business streamline initiatives our supporting financials include GAAP results as well as supplemental details on these and other charges to bring you to our pro forma or non-GAAP results. Additionally to assist you in understanding the impact of the actions we have taken this year in streamlining our business, we provided an additional schedule summarizing 2011 and 2012 quarterly sales and gross margins for our ongoing business and those we've either sold or are transitioning to a third-party model.

All of the detailed financials are attached to our press release issued today but let me add a couple of comments on the operating results. These results will be on a pro forma basis and in 2012 exclude impact of the sale of Top-Flite and Ben Hogan brand, our recent cost reduction initiatives, and non cash deferred tax valuation allowance. 2011 results exclude charges for our global operation strategy, the non cash deferred tax valuation allowance, the Top-Flite impairment, the gain on the sale of buildings and the 2011 restructuring initiatives.

For the fourth quarter sales totalled $118 million, a decrease of 23% compared to last year due to the impact of the sale of Top-Flite and Hogan businesses as well as an increase in promotional activity this year due to the slow sell-through of some of our products earlier in the year. For the full year consolidated sales were $832 million, a decrease of 6% compared to last year due to a 4% decline in our core business with the balance due to the sale of Top-Flite and Hogan businesses. Our US market accounted for 47% of full year consolidated sales with the remaining 53% coming from our international markets.

Foreign currency rates adversely impacted the 2012 sales by $5 million. Pro forma gross margins were 14% for the quarter consistent with our internal expectations and were lower than last year due to less favorable sales mix of product, the wind-down of the non-core businesses we are exiting and higher promotional activity.

On a year-to-date basis pro forma gross margins were 34% compared to 38% last year due to product mix, promotional activity related to slow product sell-through as well as higher costs on our more technical products such as the Razr Fit Driver. Pro forma operating expenses were $74 million for the quarter and were favorable compared to $79 million last year due to our recent cost-reduction initiatives. Year-to-date operating expenses totalled $353 million, a decrease of 5% compared to $373 million last year for the same reasons just mentioned.

Turning to our balance sheet we ended the quarter with cash of $52 million compared to $43 million last year. Our consolidated net receivables were $89 million, a decrease compared to $116 million last year due to the quarterly decline in sales. DSOs improved to 67 days compared to 69 days last year and the overall quality of our accounts receivables remain good.

Net inventories were $213 million, a decrease of 9% compared to last year due primarily to lower Top-Flite apparel and footwear inventories associated with our stream lining initiatives as well as a reduction in our core inventory. As a percent of trailing 12-month sales 2012 inventory was 25.5%, a slight improvement compared to 26.3% last year.

We ended the quarter with no outstanding balance on our credit facility and as of the end of the quarter we have $66 million of available credit.

Capital expenditures for the quarter were $2 million bringing the total for the full year to $18 million and depreciation and amortization expense was $8 million for the quarter bringing the total for the full year to $34 million. Both of these were slightly favorable to previous estimates. With regards to our full year of 2013 business outlook, as Chip mentioned, we estimate full years sales at this time to be $850 million. This is a 2% increase compared to our reported 2012 sales of $832 million.

Compared to our adjusted 2012 sales of our continuing core business of $772 million which excludes the businesses we exited or licensed the growth rate would be 10%. This increase in our core business sales is due to a higher mix of full priced product sales, the positive impact in Japan of adding Ryo Ishikawa to our tour staff and modest market share gains partially offsets by the negative impact of the recent weaknesses we have seen in several, currencies especially the Japanese Yen. We continue to watch FX carefully because further weakening of the yen or other currencies will increase the risk of not achieving these estimates.

Full year 2013 pro forma gross margins are estimated to be approximately 40%, an increase compared to 34% in 2012 due to improved product mix and the positive impact of exiting our non-core businesses which were diluted to our core product margins, the impact of our costs savings initiatives, and manufacturing efficiencies offset partially by higher costs associated with additional technologies in our new 2013 products.

Now, turning to our pro forma operating expenses. If you recall prior to our cost-reduction initiatives mid last year our annual OpEx run rates was about $381 million. As a result of these cost-reduction initiatives we reduced total costs by $60 million of which $41 million directly impacted operating expenses. Our 2013 pro forma forecast for operating expenses which nets these savings against the run rate of $381 million is estimated at $340 million or a reduction of 11%.

Total one-time costs associated with these initiatives are now estimated at $60 million an increase of $5 million from our last forecast. The majority of this increase is due to additional costs associated with the wind down of our Top-Flite, apparel, and GPS businesses. Two-thirds of these total one-time costs are non cash. We estimate pro forma net income at break even with a diluted loss per share due to the impact of the remaining preferred equity of $0.04 on a share count of 71 million.

The calculation of our earnings-per-share is somewhat confusing these days due to the outstanding convertible debt and convertible preferred stock outstanding. For this reason and to assist you in your models we have posted tour Investor Relations section of the Company's website a sample calculation showing how we calculate earnings-per-share. We also provided first half guidance in our press release issued today estimating sales of $555 million an increase of 7% when compared to 2012 core business sales of $519 million.

Non-GAAP first half pro forma net income of $28 million, an increase of 33% compared to $21 million last year and earnings-per-share of $0.33 compared to $0.25 last year.

Finally, we estimate capital expenditures for 2013 to range from $15 million to $20 million with depreciation and amortization of approximately $30 million.

We will now open the call for questions.

Allie, are you there? Allie.

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## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions). Your first question comes from Dan Wewer with Raymond James.

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**Dan Wewer** - *Raymond James - Analyst*

Thanks. Chip, I wanted to ask you a couple of questions regarding the outlook. First on a gross margin rate of 40% for 2013. That's still quite a bit lower than what the Company was achieving back in 2007 and 2008 and yet you're entering the new year with crystal clean inventories. So maybe if you could talk about still the difference between this 40% forecast and where the Company was back in 2007 and 2008.

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

Sure, Dan. Glad to. A couple factors on that. On the macro level what's occurred between 2007, 2008 and current is somewhat compressed gross margins is, rising costs out of Asia where we source most of our products and a increase in the amount of technology in the products such as adjustable drivers and other technologies that in many instanced are being sold at the same price points that were popular in the market in 2007, 2008. So those factors are real in our industry as candidly they are in all industries and we have to work through those. The other factor is the fact that we're still a work-in-progress here at Callaway as we go through the change effort and the improvement process that we're doing. Incredibly pleased and proud of what we've been able to accomplish in the period of time we've been able to accomplish it, but some of the improvements will take time and build momentum including operating efficiencies that factor into overhead into the costs of goods sold.

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**Dan Wewer** - *Raymond James - Analyst*

I was looking at the pricing on the X Hot driver. I believe it's $50 higher than your product that you had at that price point a year-ago.

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

That's correct.

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**Dan Wewer** - *Raymond James - Analyst*

And so are you -- so I would think that your markups could be a bit better. Are you assuming that there's still an above average amount of clearance liquidations? Impacting margin?

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

You know, we actually don't think that relative to where Callaway has been over the last several years that there is -- long story short we think our field inventories are relatively clean. And so we believe we're in an improved position there. And we think that we will have a potentially positive impact on our sell-through performance which drives those margins. You mentioned that X Hot product and that X Hot product is priced $50 higher than last year's equivalent driver, but it also includes more technology in it so when we push the limits and I say we went for more contemporary appearance and more competitive performance benefits, it includes adjustibility, it includes some PVD finishes to manufacturing techniques that sometimes raise the costs, but we believe at this stage the consumer will appreciate those and it will sell-through better.

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**Dan Wewer** - *Raymond James - Analyst*

Also I have one question on the first half revenue guidance. It looks like a 7% increase. I would have thought you would have forecasted higher than that given the Company did not have any product launches in the fourth quarter of 2011. Instead you are rolling those into the first quarter of this year. So just based on your success of the product and the change in the product launches I would think you could do better than 7%.

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

Well, the -- let me -- we forecast the second half of this year Callaway -- if you look at our 2012 numbers, Dan, we -- our sales results were relatively stronger in the first half of the year than they were in the back half of the year because we sold in relatively well. We didn't sell-through as well. And so we're anticipating next year that we will sell-through stronger which will mean the second half of the year gets a slight benefit from that perspective and also we are going to be launching product more often as I have said in the past. So this year we didn't have any product launches during the second half of the year in the US and we anticipate some product launches throughout the year this year. We also had some FX headwinds early in the year this year that we didn't have last year.

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**Dan Wewer** - *Raymond James - Analyst*

Okay. Great. Thank you.

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

Yes.

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**Operator**

Your next question comes from Scott Hamman with KeyBanc Capital Markets.

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**Scott Hamman** - *KeyBanc Capital Markets - Analyst*

Hey. Thanks. Good afternoon, guys. Just, in terms your underlying assumptions for revenue in 2013. How much are you expecting the industry to recover versus simply gaining market share gain?

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

Well, I think that -- I think it's primarily market share gains. However the US market is recovering right now and we're anticipating that trend to continue. The US market had a good year last year. It was up depending who you talked to 6% to 8% and the optimism is -- is positive for another reasonably good year and so we expect Europe to be challenged as it is -- was last year, but -- and Japan, Korea to be relatively flat to slightly up with the developing markets doing what they've been doing, developing, but the US market which is our largest market we are expecting a -- the continuation of the modest recovery that we've enjoyed and certainly the feel is that in the customers I've talked to would support that.

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**Scott Hamman** - *KeyBanc Capital Markets - Analyst*

Okay. And in terms of the retail landscape, can you quantify what your inventory levels are down in the channel year-over-year to give us a sense of -- a magnitude there and then just International versus domestic, is there a big change between those areas?

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

I can't quantify it for you, Scott. The inventory. We have that data. I don't have it at my fingertips right now, but our inventories are improved positions in most categories right now on a year-over-year basis and unfortunately, that's not -- not a quantitative answer and I didn't quite understand the second part of the question. What was that one again?

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**Scott Hamman** - *KeyBanc Capital Markets - Analyst*

Well, retail inventory levels in good shape internationally as well as domestically? Are there any areas that you're not quite satisfied with?

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

Yes, there are always areas that I'm not quite satisfied with, but yes. But on the other hand I do believe retail inventories globally are improved over recent years and I don't anticipate that being a -- a hindrance going into the year. In fact that's a positive force going into the year.

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**Scott Hamman** - *KeyBanc Capital Markets - Analyst*

Okay. And then I just have one on gross margin, a follow-up on Dan's line of questioning. Is there any way you could help us understand maybe in 2012 or in years past how much product is being sold at promotional prices or non-desirable prices and how much -- we're getting back in 2013 and what the opportunity is maybe longer-term in that dynamic?

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

You know, again, I can't quantify it for you, Scott, but whenever a company is losing market share and obviously forecasting growth, you end up with excess inventory and we have certainly had that here over the last several years and that is a considerable drain on margin performance. The key metric for our business is sell-through momentum and that is what our primary goal is this year. It clearly did a number on the margins over the last several years so you're right on the point and, unfortunately, I don't have a quantifiable answer in terms of how much of the margin erosion was discounting if you would or promotion.

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**Scott Hamman** - *KeyBanc Capital Markets - Analyst*

Okay. Great. Thanks, Chip.

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

Thank you.

**Operator**

Your next question comes from Lee Giordana with Imperial Capital.

**Lee Giordana** - *Imperial Capital - Analyst*

Thanks. Good afternoon everybody. Can you talk a little bit more about the recent changes you made in senior leadership throughout the Company and are there any other significant positions that you're still looking to make changes or fill? Thanks.

**Chip Brewer** - *Callaway Golf - Predident, CEO*

Yes. No. You know, that's one of my key accomplishments candidly for 2012 and I'm really proud of the team we've put together here at Callaway and so we as mentioned several key additions in multiple areas of the Company in addition to some changes that we brought from the inside and strong individuals that have been here for a while and I think that the result is a team that I'm very proud of and we are in place now. The senior leadership team at Callaway is complete. I'm pleased with the -- with the additions.

I'm pleased with the veterans that have been here and that was the -- among the most important jobs when I started with the Company last year. So worked very hard on that last year and I think you can start to see -- I've been talking through these analyst calls all about hope and change for the last several and you certainly can point to specifics among those changes. You're starting to see those now in the field, though.

You know, our marketing is different. If you went to the PGA show, you saw and felt a different Callaway. The product is different. In a few months they will see the upside from that perspective and that -- that was definitely a big deal, very pleased with where it ended up and happy to say that senior team is now in place and complete.

**Lee Giordana** - *Imperial Capital - Analyst*

Great. Thank you.

**Chip Brewer** - *Callaway Golf - Predident, CEO*

Thank you.

**Operator**

Your next question comes from Rommel Dionisio with Wedbush Securities.

**Rommel Dionisio** - *Wedbush Securities - Analyst*

Thank you. Chip, you mentioned in a couple of your comments I think you talked about all the technology that's going into these high end drivers. Obviously we see that from the products you're coming out with, but can you help us think about the profit margin mix change that between that and the technology going into the high end drivers plus the increased outsourcing. Is this whole mantra that we've known for years that woods and irons are still your highest profit margin category, is that still true today given all the technology that's gone into woods or has that changed a little bit here in the last year?

**Chip Brewer** - *Callaway Golf - Predident, CEO*

No it's still -- it's still. Nothing fundamentally has changed from that -- that model. The game here is the game where it is everything else. We need to make the product enough better to be able to be paid for it and also compete successfully in the marketplace. So in some of the products you're starting to see us push up some price points in the Fairway Wood we're charge $229 for the new X Hot Fairway Wood and I've got to tell you it's worth it and that is $30 higher than our Fairway Wood last year so we put some more technology into it. We, paid more for the aesthetics of it and we are not afraid to charge because it delivers on that. But our -- if you look at margins, the woods and irons are still in the relative rankings as they would have been in the past.

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**Rommel Dionisio** - *Wedbush Securities - Analyst*

Okay. Thanks very much.

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**Operator**

Your next question comes from Andrew Burns with Davidson.

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**Andrew Burns** - *Davidson - Analyst*

Thanks and good afternoon. Two questions for you here. Just following up on the comments about the US recovery and the -- the growth. Just curious in your discussion with retailers about open-to-buy dollars on the heels of a good year and what seems to be some great products. There's also a lot of noise at retail right now whether it's the consumer and weather and I just wanted to get your thoughts on open-to-buy heading into the season. Thanks.

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

I'm not hearing any issues on open-to-buy at this point. They're -- customers are relatively optimistic. We just came from the PGA show last week and the feeling was one of optimism. We think it's -- they're excited for the season to come and we're -- they've got a lot of competitive and exciting offerings including ours and as it relates to Callaway our inventories are actually in good position. So maybe -- if there's an issue out there or if they're already open-to-buy I'm not familiar with it.

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**Andrew Burns** - *Davidson - Analyst*

Great. Great. And in the prepared remarks it was mentioned that Japan and Korea gained share last year. Could you discuss the drivers of that and with the new product line it seems like there would be potential for those market share gains to accelerate in 2013 hoping to get your view there. Thanks.

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

Yes. Absolutely. And we are expecting to accelerate our market share gains in both of these key markets. Candidly we've got excellent management teams in those markets. That was -- when I went through the organization last year and met with all the individuals and did the assessments that come with that was on the list of blessings and our brand positions in those markets have been historically strong and candidly had not suffered some of the difficulties that we have in the US market.

So they started from a strong base, they have some specific product for them in the legacy line that is done historically very well. They have seen moved to some of the changes that we'll be implementing here ahead of where we are in terms of launching products during multiple times of the year, et cetera. And you know the result has been stronger performance in those markets and that ties in why we supported them the way we're doing with the investment in Ryo Ishikawa.

At the same time we being obviously very attentive to costs and we decided that we've got a great asset and opportunity over in these markets and we're going to fund those teams with that specific investment and candidly several others that we're not going to get into specifics on, to make sure that they're successful going forward. So long story short is they had some of the same tools and they just approached their businesses differently and it's been successful over there, and we are expecting growth in those markets next year in those specific markets it's going to be because of market share gains good management team and the investment in Ryo.

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**Andrew Burns** - *Davidson - Analyst*

Great. Thanks and good luck.

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

Thank you.

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**Operator**

Your next question comes from Casey Alexander with Gilford Securities.

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**Casey Alexander** - *Guilford Securities - Analyst*

Hi,good afternoon. Hey, Brad, are you -- you mentioned the potential negative effects of Forex several times. is the Company still hedging Forex at all?

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**Brad Holiday** - *Callaway Golf - CFO*

Yes, we are, Casey and it varies by currency and time of year, but we have the ability just within our own policies to hedge up to about 70% of what we would call our forward-looking business cash flow business and so we are hedged depending on the currency.

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**Casey Alexander** - *Guilford Securities - Analyst*

Okay. Secondly, the -- the Company introduced a new ball last year but is still losing some money in golf balls. Can you give me some color on the strategic plan to get that business going better and what's it going to take to break even in golf balls?

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**Chip Brewer** - *Callaway Golf - Predident, CEO*

Casey, it's Chip. Casey, we lose money in golf balls after allocations so if you -- before allocations on a direct expense basis golf balls contributes in a nice way and so we have obviously made some key operational moves in the golf ball business recently to improve our profitability from the sale of Top-Flite to the streamlining of our Chicopee operation and that's going to put us in good operating position in those markets and the next metric is pretty clean and obvious. It's to gain market share and if you look at the Callaway brand, we gained market share last year Thanks to the launch of HX Black Tour and that is going to be the engine to drive further growth going forward as other efforts to chip away at the market share gain, but the foundation and some of the changes we made last year put us in a much better operating position and we're glad to have this golf ball business. It is strategic for us and I think it's one full of opportunities.

**Casey Alexander** - *Guilford Securities - Analyst*

Two other questions. One, there seemed to be a tremendous new emphasis on social media and social media presence while I was down at the show and, secondly, there was the introduction of the new putters, the Versa putters. Can you discuss those two and where they fit within 2013?

**Chip Brewer** - *Callaway Golf - Predident, CEO*

Yes, I can. I'm really proud of both of those efforts. On the -- the social media digital space this new marketing team it's just doing a wonderful job, Casey and there's -- that's one of the changes in our world that are going on right now is that there's these avid enthusiasts that interact and engage with brands and people directly through various media such as Twitter and Facebook and Instagram and others, and our goal is to be the most open, transparent, engaging brand in the world in that space. And we've effectively gone from not in the game to among the best there and we're creating advocates and interested followers by doing that and you saw some of that firsthand at the PGA show.

So hats off to the -- the team that is driving that I call it the marketing effort. It's certainly spear-headed by that, but the total Company is behind it. It doesn't mean that with we're not going to be significant in the traditional marketing avenues because we are. You're going to see us on networks, you're going to see us on golf channel, print, etcetera, but how you play the game on the marketing side has become more evolved and we jumped in.

The Versa putters is just a cool new technology that they had underway when I got here. I got real excited about it when I saw it. It's clearly a visual technology, black-white-black, the contrast helps you line the putter up better. There's both static and dynamic benefits. It's visual on tour. It's one of those simple Aha! concepts that delivers on the benefit and will be very noticeable out there. So new technology. We've got a great line in the Odyssey product line for this year and we're optimistic on that one so I just got lucky and walked into that one.

**Casey Alexander** - *Guilford Securities - Analyst*

All right. Great. Thank you.

**Chip Brewer** - *Callaway Golf - Predident, CEO*

Thank you.

**Operator**

(Operator Instructions). Your next question is a follow-up from Dan Wewer.

**Dan Wewer** - *Raymond James - Analyst*

Chip, at the -- in your prepared comments you were calling out the X Hot Fairway Wood as the game changer for the Company. Can you remind us what portion of the addressable market is from Fairway Woods? I believe the woods category in general for Callaway is little bit less than 25% of your revenues, but I would think that a large portion of that is actually in drivers.

**Chip Brewer** - *Callaway Golf - Predident, CEO*

I would think that's correct, Patrick or Brad jump in if you want to, but in general in the market the woods category is about half drivers and up to 50% to 60% drivers and then the rest of it is Fairway Woods is slightly larger than hybrids. Is woods roughly 25%?

**Unidentified Company Representative**

Right, yes.

**Chip Brewer** - *Callaway Golf - Predident, CEO*

Okay. So you've got that correct but having said that, it's a profitable category, it's an important category. We have seen by others example last year, Dan, that Fairway Woods can actually drive sales of other product. Fairway Woods were a historical strong position for Callaway and it was a market share leader in the Fairway Wood category potentially up until last year and where we weren't in the game and -- and the product that we're introducing this year I have already gushed on about is -- is phenomenal. I believe it's the best fairway wood in golf and the team wowed me that they could get that done in the time period that I gave them to do it.

**Dan Wewer** - *Raymond James - Analyst*

So is it more difficult to tell a performance story in drivers nowadays given the limits on drivers from the -- the golf -- the USGA and so forth is that why.

**Chip Brewer** - *Callaway Golf - Predident, CEO*

We have to -- we ran into our limit on COR in size in drivers so the two big trends that you saw driving some driver innovation and -- replacement cycle out there was the size of the driver and the COR of the driver and they're maxed out now in size and COR and Fairway Woods are not there yet although our Fairway Wood is at the legal limit and my position is ours is the only one.

**Dan Wewer** - *Raymond James - Analyst*

Just one other follow-up that you had called out TaylorMade putting some excitement in Fairway Woods last year and it looks like now they're taking that story into irons with their RocketBladez. Does Callaway have a -- do you have a product that would compete against the RocketBladez or is that something a product line that comes out for out later this year?

**Chip Brewer** - *Callaway Golf - Predident, CEO*

We have -- you know, I'm not going to comment on others specifically and TaylorMade clearly has done a great job. I have a lot of respect for that organization, but on the iron side we have big plans in the iron category. Callaway was the leader in the irons category from a market share basis up until just a few years ago. We've got a lot of equity and a lot of potential in that space. Our X hot irons that we're launching this year are a completely retooled effort to regain market share in that category.

If you looked at our 2012 line it was confusing and everybody told us that. We made -- we had six or seven irons all named Razr and no clear performance benefit that cut through. Our X Hot irons are combining what we've always had, which is the overall total performance, ease of hitting et cetera but with a re-energized emphasis on distance. We believe we will be longer than any other iron out there and we're going to make that benefit claim as part of our marketing communications. So it doesn't matter who we're competing against from that space. We think we've got the answer on that product line as well and it is the X Hot iron.

**Dan Wewer** - *Raymond James - Analyst*

Okay. Great. Thank you.

**Operator**

Your final question comes from Craig Kennison with Robert W. Baird.

**Craig Kennison** - *Robert W. Baird - Analyst*

Good afternoon. Thanks for taking my question as well. One I wanted to follow up on the tour strategy. It sounds like there's more to come there, but maybe you would address more broadly your philosophy and whether you plan to get perhaps younger and more global or how would you identify your philosophy of tour?

**Chip Brewer** - *Callaway Golf - Predident, CEO*

I think tour is a very important part of our turnaround story. I think it's an important part of the marketing message and so I'm a big believer in that space and what it does for the brand and the Company. You are correct our efforts that you saw here in 2013 are our first step. We will get I believe stronger and even bigger out on tour and I'm obviously very pleased to have Phil and Ernie. They're awesome and I love also adding these new young bombers to it to complement the strong position we've had.

From a global basis I actually think the Company has been phenomenal. Our European tour presence is a strength. We've had strong positions in Asia, Ryo Ishikawa is you know a rock star in Japan, but you will continue to see a dedicated commitment and energy on the tour front from Callaway Golf going forward.

**Craig Kennison** - *Robert W. Baird - Analyst*

Thank you. And as a follow-up would you say your total spend on tour would be roughly the same and you're just reallocating resources, or do you think there is an opportunity to get more return by spending more?

**Chip Brewer** - *Callaway Golf - Predident, CEO*

In the future I think that as the business continues to make progress we'll continue to invest accordingly and tour will be part of that.

**Craig Kennison** - *Robert W. Baird - Analyst*

Terrific. Thank you.

**Operator**

At this time there are no further questions. Mr. Brewer, do you have any closing remarks?

**Chip Brewer** - *Callaway Golf - Predident, CEO*

Certainly. Thank you. I just want to thank everybody for calling in today. Your participation and interest is appreciated. We're obviously delighted to be entering the 2013 season and I look forward to reporting on our results with you in a few months. Thanks very much for calling in.

**Operator**

Ladies and gentlemen, this does conclude today's conference call. Thank you for your participation. You may now disconnect.