

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 1998
COMMISSION FILE NUMBER 1-11893

GUESS ?, INC.

(Exact name of registrant as specified in its charter)

DELAWARE
(State or other jurisdiction
of incorporation or organization)

95-3679695
(I.R.S. Employer Identification
Number)

1444 SOUTH ALAMEDA STREET
LOS ANGELES, CALIFORNIA 90021
(213) 765-3100

(Address, including zip code, and telephone number, including area code)

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

TITLE OF EACH CLASS	NAME OF EACH EXCHANGE ON WHICH REGISTERED
Common Stock, par value \$0.01 per share	New York Stock Exchange

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

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

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

As of February 26, 1999, the aggregate market value of the voting and non-voting common equity stock held by non-affiliates of the registrant was \$48,703,985.

As of February 26, 1999, the registrant had 42,911,035 shares of Common Stock outstanding.

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PART I

ITEM 1. BUSINESS

IMPORTANT FACTORS REGARDING FORWARD-LOOKING STATEMENTS

Various forward-looking statements have been made in this Form 10-K. Forward-looking statements may also be in the registrant's other reports filed under the Securities Exchange Act of 1934, in its press releases and in other documents. In addition, from time to time, the registrant through its management may make oral forward-looking statements.

Forward-looking statements generally refer to future plans and performance, and are identified by the words "believe," "expect," "anticipate," "optimistic," "intend," "aim," "will" or similar expressions. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of which they are made. The registrant undertakes no obligation to update publicly or revise any forward-looking statements.

For additional information regarding forward-looking statements, refer to Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations.

GENERAL

Guess ?, Inc. ("the Company" or "Guess"), founded in 1981 by the Marciano brothers, designs, markets, distributes and licenses one of the world's leading lifestyle collections of casual apparel, accessories and related consumer products. The Company's apparel for men, women and girls is marketed under numerous trademarks including Guess, Guess?, Guess U.S.A., Guess Collection and Guess? and Triangle Design. The lines include full collections of denim and cotton clothing, including jeans, pants, overalls, skirts, dresses, shorts, blouses, shirts, jackets and knitwear. In addition, the Company has granted licenses to manufacture and distribute a broad range of products that complement the Company's apparel lines, including clothing for infants and children, activewear, footwear, eyewear, watches, home products and other fashion

accessories. Revenue generated from wholesale and retail operations and from licensing activities, were 45.0%, 47.2% and 7.8%, respectively, of net revenue in 1998. The Company's total net revenue in 1998 was \$471.9 million and net earnings were \$25.1 million.

BUSINESS STRENGTHS

The Company believes it possesses a foundation of business strengths necessary for the execution of its business growth strategies. These business strengths include the following:

BRAND EQUITY. GUESS? believes that its well-developed and highly recognizable brand is one of the Company's most valuable assets. Through its award-winning advertising, under the creative leadership and vision of Paul Marciano, the Company has achieved worldwide recognition of the GUESS? brand name. It has developed the "GUESS? signature image" and "GUESS? lifestyle concept," through the use of its strong and distinctive images, merchandising display themes, logos, and trademarks which are registered in over 160 countries. By retaining control over its advertising and marketing activities from its headquarters in Los Angeles, the Company maintains the integrity, consistency and direction of the GUESS? brand image worldwide, while realizing substantial cost savings when compared to the use of outside advertising agencies.

PRODUCT DESIGN. The enduring strength of the GUESS? brand name and image is due mainly to the Company's consistent emphasis on innovative and distinctive product designs that stand for exceptional styling and quality. Under the direction of Maurice Marciano, the Company's design function is performed by an in-house staff, which is structured to deliver synergy and consistency in its product offerings and design direction. The apparel industry is highly competitive and subject to rapidly changing consumer preferences and tastes. The GUESS? design team seeks to anticipate, adapt and respond to these changing

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preferences by aggressively monitoring emerging fashion trends, while retaining the distinctive GUESS? image. Design concepts are inspired by an appreciation of the American lifestyle combined with a European flair.

ADVERTISING AND MARKETING. All worldwide advertising, marketing activities and promotional materials are controlled from the Company's headquarters in Los Angeles. Guess Jeans, Guess U.S.A. and Guess?, Inc. images have been showcased in dozens of major publications, and outdoor and broadcast media throughout the United States and worldwide. The Company's advertising campaigns promote the GUESS? image and products, with an emphasis on image. The Company's signature black and white print advertisements, as well as color print advertisements, have garnered prestigious awards including Clio, Belding and Mobius awards for creativity and excellence. GUESS? has maintained a high degree of consistency in its advertisements, by using similar themes and images. The Company requires its licensees and distributors to invest a percentage of their net sales of licensed products and net purchases of GUESS? products, respectively, in Company-approved advertising, promotion and marketing.

LICENSING OPERATIONS. The desirability of the GUESS? brand name among consumers has allowed the Company to selectively expand its product offerings and global markets through licensing arrangements, with minimal capital investment or on-going operating expenses. The Company carefully selects its licensees and maintains strict control over product design, advertising, marketing and distribution of all licensed products in order to maintain consistent global brand equity. The Company currently has 32 licenses that include watches, eyewear, shoes, jewelry and related accessories. The Company has granted licenses for the manufacture and sale of GUESS? branded products in markets which include Europe, Asia, South America, Australia and Africa.

WHOLESALE DISTRIBUTION. The Company has both domestic and international wholesale distribution channels. Domestic wholesale customers consist primarily of better department stores and select upscale specialty stores, which have the image and merchandising expertise that GUESS? requires for the effective

presentation of its products. Leading domestic wholesale customers include Federated Department Stores, Inc., The May Department Stores Company, Dillard's, Inc. and Dayton Hudson Corporation. Through its wholesale distribution channel to larger customers with locations throughout the United States, the Company's products reach a broad geographic market. During 1998, the Company's products were sold directly to consumers from approximately 2,800 retail store locations in the United States. These locations include approximately 1,200 shop-in-shops, an exclusive selling area within a department store that offers a wide array of GUESS? products and incorporates GUESS? signage and fixture designs. These shop-in-shops allow the Company to reinforce the "GUESS? signature image" and "GUESS? lifestyle concept" with its customers. Additionally, via its foreign subsidiaries and network of international distributors, the Company's products are found in major cities throughout Asia, Europe, South America and the Middle East.

RETAIL DISTRIBUTION. As of December 31, 1998, the Company's domestic retail operations consisted of 84 retail and 48 company outlet stores that were owned and operated directly by the Company. Distribution through the Company's retail stores allows the Company to influence the merchandising and presentation of its products, build brand equity and to test market new product design concepts. The Company further enhances the GUESS? image through its retail network, which creates an upscale and inviting shopping environment. The Company's 84 domestic retail stores carry a full assortment of men's and women's GUESS? merchandise, including most of its licensed products. The Company's 48 domestic company outlet stores are located in outlet malls and strip centers, generally operating outside the shopping radius of the Company's wholesale customers and its own retail stores. These stores sell selected styles of GUESS? apparel and licensed products at a discount to value-conscious customers.

FINANCIAL STRENGTH. The Company's financial position improved dramatically during 1998, as total debt was reduced by \$42.5 million to \$99.0 million at year-end. The Company also has a \$100.0 million revolving credit facility that was completely paid off by the end of 1998. In addition, at the end of 1998, the

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Company had \$11.9 million in short-term investments. The Company anticipates it will be able to satisfy its ongoing cash requirements through 1999, including expansion plans, primarily with cash flow from operations, supplemented, if necessary, by borrowings under its revolving credit facility.

BUSINESS GROWTH STRATEGIES

The Company regularly evaluates and implements initiatives that it believes will build brand equity, grow operations and increase profitability. The following is a summary of these key growth strategies.

BUILDING BRAND EQUITY. The Company views the value of its brand as a strategic asset and a primary source of sustainable competitive advantage. Elements contributing to brand equity include brand loyalty, name awareness, perceived quality, strong brand images, public relations, publicity, promotional events and trademarks. In order to build long-term brand equity the Company will launch a new marketing campaign in 1999, which will include Internet advertising sponsors and television commercials, strong and consistent images utilized in all media forms, fresh merchandising presentation themes and enhanced point-of-sale materials. This marketing program is designed to convey a uniform style image for the brand, aimed at increasing the desire of the target group to join the GUESS? customer group.

REPOSITIONING LICENSEE PORTFOLIO. In order to maintain quality and control of the brand, the Company will continue to strategically reposition its licensing portfolio by bringing in-house apparel licenses, where appropriate. Over the past few years, the Company has been encouraged by the results of converting the Women's Knits and Girl's product lines. The Company believes this process creates improved synergy and consistency of its overall apparel product offerings. It also plans to enhance the effectiveness of its existing licensees by continuing to provide design, production, technical and marketing assistance and direction, while pursuing efficiencies of scale through joint sourcing,

whenever possible.

IMPROVED PRODUCT SOURCING. The Company is refocusing its product sourcing strategies to increase efficiencies, reduce costs and improve quality. Commencing in 1998, the Company increased its utilization of lower-cost, offshore "packaged purchases," in which it supplies the product design and fabric selection, and the vendor manufactures and delivers the finished product. On an increasing basis, the Company will seek to strategically align itself with sourcing vendors worldwide, who will take full responsibility for delivering a quality, finished product in a timely manner. The trend towards increasing offshore package purchase production will continue throughout 1999. The Company will continue to use a limited number of local contractors, as it is important to react to last minute trends, as well as respond to rush reorders. By increasing the use of packaged programs, the Company believes it can achieve improved product gross margins, reduce carrying costs of raw materials and improve deliveries and quality.

EXPAND SHOP-IN-SHOP PROGRAMS. The GUESS? "shop-in-shop" concept is designed to enhance the presence and brand awareness of GUESS? products in department stores. The strategic product presentation, theme-based fixturing, displays, strong and distinctive images and point-of-sale materials in these shops are designed to reinforce and capitalize on the "GUESS? lifestyle" concept in these premium department store locations. These shops also facilitate ease of consumer shopping by featuring a comprehensive presentation of the Company's merchandise. The Company intends to open and/or remodel up to 125 shops during 1999, featuring a fresh shop fixture design concept and presentation theme. The Company intends to open and/or remodel up to an additional 200 shops during 2000.

RETAIL STORE STRATEGY AND EXPANSION PLANS. The Company's primary retail strategies for achieving greater store profitability are three-fold: aggressively manage inventory, create a team of motivated sales associates and build brand equity. By pro-actively managing our product mix through the aggressive monitoring of sell-through rates, timely product deliveries and earlier disposal of past-season fashion items, the Company believes it can capitalize on emerging trends and that its customers will respond favorably to its "fashion-right" products. The Company is dedicated to improving customer service and creating a more favorable shopping experience for customers by continuing to develop teams of highly

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motivated and service-oriented sales associates. We plan to accomplish this through sales training, enhanced incentives, and expanded product knowledge.

The look and feel of GUESS? retail and outlet stores play an important role in building the Company's brand equity. In order to enhance its quality of presentation, the Company plans to remodel approximately 20 stores during 1999. In addition, the Company will continue to enhance its presentation of strong and distinctive visual imagery, themed fixtures and point-of-sale displays. This environment, combined with the synergistic presentation of a wide array of fresh GUESS? and licensee-produced product offerings, including men's, women's, Guess Collection, shoes, eyewear, watches, jewelry and related accessories, showcases the "GUESS? lifestyle" concept in its entirety.

The Company's retail growth strategy is to increase domestic retail sales and profitability by expanding its network of retail stores and improving the performance of existing stores. In 1998, the Company intentionally slowed the expansion of its retail network until the aforementioned strategies to improve store operations and merchandising produced more favorable results. During 1999, the Company plans to expand its 132 existing store base by opening 10 new stores and improve its operating base by closing underperforming stores. During 2000, the Company plans to resume retail expansion by increasing retail space by up to 20%.

LEVERAGING THE INTERNET. The Company's latest venture is the development of the GUESS? on-line retail superstore to capitalize on the growth of the Internet and emerging technologies. The new "guess.com" will be rolled out in multiple

phases throughout 1999, beginning in the second quarter. The Company has licensed Interworld Corporation's Commerce Exchange solution to power the Web site, which will showcase GUESS? products in an easy-to-navigate, on-line catalog and allow customers to view and purchase its collections of casual apparel and accessories. This virtual store is designed to, among other things, create an additional retail distribution channel, build brand equity, expand market penetration, improve customer service levels and create a fun and entertaining alternative-shopping environment. Later phases of the project are expected to involve business-to-business solutions, which are designed to expand and enhance the Company's domestic wholesale distribution channel, whereby the Company's domestic wholesale customers will be able to place their orders via the Internet. This should reduce operating costs, increase sourcing and distribution efficiencies, and improve customer service.

COMPANY PRODUCTS

The Company derives its net revenue from three primary sources: the sale of Guess men's, women's and girl's apparel worldwide to wholesale customers and distributors, from the sale of Guess men's, women's and girl's apparel and its licensees' products through the Company's network of retail and factory outlet stores primarily in the United States and net royalties from worldwide licensing activities. The following table sets forth the net revenue of the Company through its channels of distribution.

	YEAR ENDED DECEMBER 31,					
	1998		1997		1996	
	(IN THOUSANDS)					
Net Revenue:						
Retail operations.....	\$ 222,624	47.2%	\$ 215,873	41.9%	\$ 209,828	38.1%
Wholesale operations.....	212,504	45.0	250,040	48.5	288,046	52.2
Net revenue from product sales.....	435,128	92.2	465,913	90.4	497,874	90.3
Net royalties.....	36,803	7.8	49,459	9.6	53,288	9.7
Total net revenue.....	\$ 471,931	100.0%	\$ 515,372	100.0%	\$ 551,162	100.0%

PRODUCTS. The Company's apparel products are organized into three primary categories: men's, women's and girl's apparel. A major portion of the Company's men's, women's and girl's apparel lines consists of basic, recurring styles which the Company believes are less susceptible to fashion obsolescence and are less seasonal in nature than fashion product styles. Basic product styles provide the Company with a base of business that usually carries over from season to season and year to year. Basic products are primarily made of denim and include jeans, skirts, dresses, overalls and shorts in a variety of fits, washes and styles. To take advantage of contemporary trends, the Company complements its basic styles with more fashion-oriented items. Fashion products range in style from contemporary sportswear to casual apparel and include colored denim items, pants, shirts, jackets and knitwear made of a variety of materials including fine cotton, man-made fabric and leather. A limited number of best-selling fashion items in a collection may be included in one or more subsequent collections, and a select few may be added to the Company's basic styles.

The Company's line of women's apparel also includes the Guess Collection product line, a collection of women's skirts, tops, jackets, blazers and blouses incorporating a sophisticated combination of colors and styles. These products are currently sold virtually exclusively through the Company-owned and -operated retail stores and are primarily designed to appeal to the contemporary segment of the apparel market.

LICENSED PRODUCTS. The high level of desirability of the Guess brand name among consumers has allowed the Company to selectively expand its product offerings and distribution channels worldwide through licensing arrangements. The Company currently has 32 licenses. Worldwide sales of licensed products (as

reported to the Company by its licensees) were approximately \$577 million in 1998. The Company's net royalties from such sales, including fees from new licensees, were \$36.8 million in 1998. Approximately 50% of the Company's gross royalties were derived from its top four licensed product lines in 1998.

DESIGN

Under the direction of Maurice Marciano, Guess garments are designed by an in-house staff of four design teams (men's, women's, girl's and Guess Collection) located in Los Angeles, California. Guess design teams travel throughout the world in order to monitor fashion trends and discover new fabrics. Fabric shows in Europe, Asia and the United States provide additional opportunities to discover and sample new fabrics. These fabrics, together with the trends uncovered by the Company's designers, serve as the primary source of inspiration for the Company's lines and collections. The Company also maintains a fashion library consisting of antique and contemporary garments as an additional source of creative concepts. In addition, design teams regularly meet with members of the sales, merchandising and retail operations to further refine the Company's products in order to meet the particular needs of the Company's markets.

DOMESTIC WHOLESALE CUSTOMERS

The Company's domestic wholesale customers consist primarily of better department stores and select upscale specialty stores, which have the image and merchandising expertise that Guess requires for the effective presentation of its products. Leading wholesale customers include Federated Department Stores, Inc., The May Department Stores Company and Dillard's, Inc., among others. During 1998, the Company sold its products directly to approximately 2,800 retail doors within the United States.

A key element of the Company's merchandising strategy is the shop-in-shop merchandising format, an exclusive selling area within a department store that presents a full array of Guess products using Guess signage and fixture designs. At December 31, 1998, there were approximately 1,200 shop-in-shops (excluding shop-in-shops installed by licensees and distributors) that feature Guess products (other than

the Guess Collection and Girls). The Company intends to add or remodel approximately 125 shop-in-shops by the end of 1999.

Sales representatives are located in the Company's showrooms in New York, Los Angeles, Dallas, Chicago, Italy and Hong Kong. They coordinate with customers the inventory level and product mix that should be carried in each store to maximize retail sell-through and enhance the customers' profit margins. Such inventory level and product mix are then used as the basis for developing sales projections and product needs for each wholesale customer and scheduling production. Additionally, the Company employs merchandise coordinators, who work with the store to ensure that the Company's products are appropriately displayed.

Certain of the Company's domestic wholesale customers, including some under common ownership, have accounted for significant portions of the Company's net revenue. During 1998, Bloomingdale's, Macy's and other affiliated stores owned by Federated Department Stores, Inc. together accounted for approximately 9.5% of the Company's net revenue. During the same period, Dillard's, Inc. and The May Department Stores Company accounted for approximately 5.6% and 4.8% of the Company's net revenue, respectively.

DOMESTIC RETAIL OPERATIONS

At December 31, 1998, the Company's domestic retail operations consisted of 84 retail and 48 factory outlet stores owned and operated directly by Guess in the United States, which principally sell Guess label products. Guess retail stores outside the United States, with the exception of the Company-owned and -operated store in Florence, Italy, are owned and operated by the Company's

distributors and licensees. See "International Business". Since the beginning of 1994 through December 31, 1998, the Company has opened a total of 63 retail stores and 16 factory outlet store and has closed 15 retail and 15 factory outlet stores. The percentage of net revenue generated by the retail network has increased from 27.2% to 51.2% of the Company's net revenue from product sales from 1994 through 1998.

RETAIL STORES. The Company's 84 domestic retail stores range in size from approximately 2,000 to 10,000 square feet. The Company's retail stores carry a full assortment of men's and women's Guess merchandise, including most of its licensed products. During 1998, the Company opened one retail store and closed two retail stores. The Company plans to open up to seven retail stores during 1999. The planned slow-down in the roll-out of new retail stores during 1998 and 1999 is primarily due to the Company's desire to continue focusing its efforts on improving the profitability and efficiency of existing stores.

FACTORY OUTLET STORES. The Company's 48 domestic factory outlet stores range in size from approximately 3,500 to 8,900 square feet and are located in outlet malls and strip centers generally operating outside the shopping radius of the Company's wholesale customers and its retail stores. These stores sell selected styles of Guess apparel and licensed products at a discount to value-conscious customers. During 1998, the Company opened two and closed three factory stores. The Company plans to open up to three and close three factory outlet stores in 1999.

INTERNATIONAL BUSINESS

Guess derives net revenue and earnings outside the United States from two principal sources: (i) sales of Guess brand apparel directly to 17 foreign distributors who distribute such apparel to better department stores, upscale specialty retail stores and Guess-licensed retail stores operated by Guess distributors or licensees and (ii) royalties from licensees who manufacture and distribute Guess brand products outside the United States.

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The Company sells products through distributors and licensees throughout Asia, South America, Europe, South Africa, Australia and the Middle East.

At December 31, 1998, 257 Guess retail and outlet stores were owned and operated internationally by licensees and distributors. The Company's retail store license agreements generally provide detailed guidelines for store fixtures, merchandising and marketing programs. The appearance, merchandising and service standards of these stores are closely monitored to ensure the Guess image is maintained. The Company has been advised by its distributors and licensees that they plan to open a net of 15 new stores in 1999. Guess also owns and operates a flagship Guess retail store located in Florence, Italy.

LICENSE AGREEMENTS AND TERMS

The Company's manufacturing license agreements customarily provide for a three-to five-year initial term with a possible option to renew prior to expiration for an additional multi-year period. In addition to licensing products which complement the Company's apparel products, Guess has granted licenses for the manufacture and sale of Guess branded products similar to the Company's, including men's and women's denim and knitwear, in markets such as the Philippines, Canada, Argentina, Mexico, Chile, South Africa, South Korea, Brazil and Japan. Licenses granted to certain licensees which have produced high-quality products and otherwise have demonstrated solid operating performance, such as Guess Watches and Guess Eyewear, have been renewed and in some cases expanded to include new products or markets. The typical license agreement requires that the licensee pay the Company the greater of a royalty based on a percentage of the licensee's net sales of licensed products or a guaranteed minimum royalty that typically increases over the term of the license agreement. Generally, licensees are required to spend a percentage of the net sales of licensed products for advertising and promotion of the licensed products. In addition, certain licensees are required to contribute toward the protection of the Company's trademarks within the territories granted to such

licensees, thereby assisting Guess in its efforts to prevent counterfeiting and other trademark infringement in such territories.

The Company's Licensing Department strictly monitors product design, development, merchandising and marketing. All Guess brand products, advertising, promotional and packaging materials must be approved in advance by Guess. The Licensing Department meets regularly with licensees to ensure consistency with Guess's overall marketing, merchandising and design strategies, and to ensure uniformity and quality control.

In addition to the retail stores operated outside of the United States as mentioned above in the "International Business" section, Guess licensees operate 27 retail and outlet stores in the United States.

ADVERTISING AND MARKETING

The Company's advertising, public relations and marketing strategy is to promote a consistent high impact image which endures regardless of changing consumer trends. Since the Company's inception, Paul Marciano has had principal responsibility for the Guess brand image and creative vision. All worldwide advertising and promotional material is controlled through the Company's Advertising Department based in Los Angeles. Guess Jeans, Guess U.S.A. and Guess Inc. images have been showcased in dozens of major publications, and outdoor and broadcast media throughout the United States and the world.

The Company's advertising strategy promotes the Guess image and products, with an emphasis on image. The Company's signature black and white print advertisements, as well as color print advertisements, have garnered prestigious awards, including Clio, Belding and Mobius awards for creativity and excellence. Such awards, which the Company has received on numerous occasions, are generally awarded based on the judgment of prominent members of the advertising industry. Guess has maintained a high degree of consistency in its advertisements, using similar themes and images. The Company requires its licensees and distributors to invest a percentage of their net sales of licensed products and net purchases of Guess products, respectively, in approved advertising, promotion and marketing.

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The Company's in-house Advertising Department is responsible for media placement of all advertising worldwide, which includes approval of all advertising campaigns from its licensees and distributors. The Company uses a variety of media which emphasizes print and outdoor advertising. The Company has focused advertisement placement in national and international contemporary fashion/beauty and lifestyle magazines including Vanity Fair, Harpers Bazaar, Elle, W and Details. By retaining control over its advertising programs, the Company is able to maintain the integrity of the Guess brand image while realizing substantial cost savings when compared to the use of outside agencies.

The Company further strengthens communications with customers through Guess Interactive, the Company's Web site (<http://www.guess.com>). This global medium enables the Company to provide timely information in an entertaining fashion to consumers on the Company's history, Guess products and store locations and allows the Company to receive and respond directly to customer feedback.

SOURCING AND PRODUCT DEVELOPMENT

The Company sources products through numerous suppliers, many of whom have established relationships with the Company. The Company seeks to achieve the most efficient means for timely delivery of its high quality products. The Company's fabric specialists work with fabric mills in the United States, Europe and Asia to develop woven and knitted fabrics that enhance the products' comfort, design and appearance. For a substantial portion of the Company's apparel products, production planning takes place generally four to five months prior to the corresponding selling season. Delivery of certain basic products are generally accomplished through the Company's Quick Response EDI (Electronic Data Interchange) replenishment system which ensures shipment of such products generally within 48 hours of receipt of customer orders.

The Company does not own any production equipment other than cutting machinery. The Company engages in global sourcing for its production. In order to remain competitive, in recent years, Guess has increasingly been sourcing its finished products globally. The Company now sources a majority of its finished products from third-party suppliers located outside the United States. The majority of these finished products are acquired as package purchases where the Company supplies the design and fabric selection and the vendor supplies the finished product. Although the Company has long-term relationships with many of its vendors, it does not have long-term written agreements with them. The production and sourcing staffs in Los Angeles oversee aspects of apparel manufacturing, quality control and production, as well as research and develop new sources of supply.

The Company's products use a variety of raw materials, principally consisting of woven denim, woven cotton and knitted fabrics and yarns. Historically, the Company has had to make commitments for a significant portion of its fabric well in advance of sales. By increasing the use of packaged purchases, the Company is able to reduce its raw materials inventory. As the Company transitions to sourcing substantially all of its finished products through packaged purchases, it expects to sell existing raw materials to certain of its package purchase vendors. This transitional raw materials sell-off period is expected to last through the first half of 1999. Thereafter, the Company's package purchase providers would purchase raw materials directly from vendors. Accordingly, the Company's risk of fabric obsolescence will be reduced due to the declining levels of raw materials inventory.

QUALITY CONTROL

The Company's quality control program is designed to ensure that products meet the Company's high quality standards. The Company monitors the quality of its fabrics prior to the production of garments and inspects prototypes of each product before production runs commence. The Company also performs random in-line quality control checks during and after production before the garments leave the contractor. Final random inspections occur when the garments are received in the Company's distribution centers.

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The Company believes that its policy of inspecting its products at its distribution centers and at the vendors' facilities is important in maintaining the quality and reputation of its products.

WAREHOUSE AND DISTRIBUTION CENTERS

The Company utilizes distribution centers at three strategically located sites. Distribution of the Company's products in the United States is centralized in the Los Angeles, California facility which is leased from a related party and operated by the Company. The Company also holds a 10% ownership interest in a licensee which operates a distribution center in Florence and services Europe. Additionally, the Company utilizes a contract warehouse in Hong Kong which services the Pacific Rim.

In order to ensure that each of its retail customers receive merchandise in satisfactory condition, substantially all Company products are processed through one of the Company's distribution centers before delivery to the retail customer. Each customer is assigned to one of the Company's distribution centers, depending on the customers' location.

At its distribution center in Los Angeles, the Company has also developed a fully integrated and automated distribution system. The bar code scanning of merchandise, picking tickets and distribution cartons, together with radio frequency communications, provide timely, controlled, accurate and instantaneous updates to the distribution information systems.

COMPETITION

The apparel industry is highly competitive and fragmented, and is subject to

rapidly changing consumer demands and preferences. The Company believes that its success depends in large part upon its ability to anticipate, gauge and respond to changing consumer demands and fashion trends in a timely manner and upon the continued appeal to consumers of the Guess image. Guess competes with numerous apparel manufacturers and distributors and several well-known designers which have recently entered or re-entered the designer denim market. The Company's retail and factory outlet stores face competition from other retailers, including some of the Company's major wholesale customers. The Company's licensed apparel and accessories also compete with a substantial number of designer and non-designer lines and various other well-known brands. Many of the Company's competitors have greater financial resources than Guess. Although the level and nature of competition differ among its product categories, Guess believes that it competes on the basis of its brand image, quality of design, workmanship and product assortment.

TRADEMARKS

The Company owns numerous trademarks, including Guess?, Guess, Guess? and Triangle Design, Baby Guess, Guess Kids, Guess U.S.A. and Guess Collection. At December 31, 1998, the Company had more than 2,700 U.S. and international registered trademarks or trademark applications pending with the trademark offices of the United States and in over 165 countries around the world. From time to time, the Company adopts new trademarks in connection with the marketing of new product lines. The Company considers its trademarks to have significant value in the marketing of its products and acts aggressively to register and protect its trademarks worldwide.

Like many well-known brands, the Company's trademarks are subject to infringement. Guess has a staff devoted to the monitoring and aggressive protection of its trademarks worldwide.

WHOLESALE BACKLOG

The Company maintains a model stock program in its basic denim products which allows Guess to generally replenish a customer's inventory within 48 hours. Guess generally receives orders for its fashion apparel 90 to 120 days prior to the time the products are delivered to stores. At February 28, 1999, the

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Company had unfilled wholesale orders, consisting primarily of orders for fashion apparel, of approximately \$93.9 million, compared to \$76.7 million for such orders at March 1, 1998. Guess expects to fill substantially all of these orders in 1999. The backlog of wholesale orders at any given time is affected by various factors, including seasonality and the scheduling of manufacturing and shipment of products. Accordingly, a comparison of backlogs of wholesale orders from period to period is not necessarily meaningful and may not be indicative of eventual actual shipments.

EMPLOYEES

Guess believes that its employees ("associates") are one of its most valuable resources. At December 31, 1998, there were approximately 3,200 associates. Associates include approximately 900 and 2,300 in wholesale operations and retail operations, respectively.

Guess is not a party to any labor agreements and none of its associates are represented by labor unions. The Company considers its relationship with its associates to be good. However, the Company is currently the target of a corporate campaign by the Union of Needletrades Industrial and Textile Employees ("UNITE"), whose campaign is intended, in part, to organize a portion of the Company's manufacturing employees. In addition, the Company was among the first in the apparel industry to implement a program to monitor the compliance of subcontractors with Federal minimum wage and overtime pay requirements. See "Item 3. Legal Proceedings."

ENVIRONMENTAL MATTERS

The Company is subject to federal, state and local laws, regulations and ordinances that (i) govern activities or operations that may have adverse environmental effects (such as emissions to air, discharges to water, and the generation, handling, storage and disposal of solid and hazardous wastes) or (ii) impose liability for the costs of clean up or other remediation of contaminated property, including damages from spills, disposals or other releases of hazardous substances or wastes, in certain circumstances without regard to fault. Certain of the Company's operations routinely involve the handling of chemicals and wastes, some of which are or may become regulated as hazardous substances. The Company has not incurred, and does not expect to incur, any significant expenditures or liabilities for environmental matters. As a result, the Company believes that its environmental obligations will not have a material adverse effect on its financial condition or results of operations.

ITEM 2. PROPERTIES

Certain information concerning Guess's principal facilities, all of which are leased, is set forth below:

LOCATION	USE	APPROXIMATE AREA IN SQUARE FEET
1444 South Alameda Street Los Angeles, California	Principal executive and administrative offices, design facilities, sales offices, distribution and warehouse facilities, production control, and sourcing	565,000
1385 Broadway New York, New York	Administrative offices, public relations, and showrooms	30,000
Kowloon, Hong Kong	Distribution and licensing coordination control	3,000
Florence, Italy	Administrative office and retail store	4,100

The Company's corporate, wholesale and retail headquarters and its production, warehousing and distribution facilities are located in Los Angeles, California and consist of seven adjacent buildings and one remote storage facility, totaling approximately 565,000 square feet. Certain of these facilities are leased

from limited partnerships in which the sole partners are trusts controlled by and for the benefit of Maurice Marciano, Paul Marciano and Armand Marciano and their families (the "Principal Stockholders") pursuant to leases that expire in July 2008. The total lease payments to these limited partnerships are \$236,000 per month with aggregate minimum lease commitments to these partnerships at December 31, 1998 totaling approximately \$25.3 million. See "Item 13. Certain Relationships and Related Transactions."

Guess leases its showrooms, advertising, licensing, sales and merchandising offices, remote warehousing facility and retail and factory outlet store locations under non-cancelable operating lease agreements expiring on various dates through May 2012. These facilities are located principally in the United States, with aggregate minimum lease commitments, at December 31, 1998, totaling approximately \$192.6 million.

As of December 31, 1998, the terms of the Company's store leases, excluding renewal options, expire as follows:

YEARS LEASE TERMS EXPIRE	NUMBER OF STORES
1999-2001.....	20
2002-2004.....	49
2005-2007.....	58
2008-2010.....	4
Thereafter.....	1

Guess believes that its existing facilities are well maintained, in good operating condition and are adequate to support its present level of operations. See Notes 8 and 9 of Notes to Consolidated Financial Statements for further information regarding current lease obligations.

ITEM 3. LEGAL PROCEEDINGS

On August 7, 1996, a class action complaint naming the Company and certain of its independent contractors was filed in the Superior Court of the State of California for the County of Los Angeles, titled as Brenda Figueroa et. al. v. Guess ?, Inc. et. al. (Case No. BC 155 165). In this case, an alleged class action, plaintiffs assert claims for violation of state wage and hour laws, wrongful discharge, and breach of contract arising out of the Company's relationship with its independent contractors and actions taken by the Company's independent contractors with respect to the employees of such independent contractors. Plaintiffs also allege that the Company breached its agreement with the United States Department of Labor regarding the monitoring of its independent contractors. The Court has held two hearings on certifying the alleged class. While the Court has not announced a final ruling, the Court has indicated it likely will at least certify a class of plaintiffs who allege wrongful termination claims.

The Union of Needletrades, Industrial and Textile Employees ("UNITE") has filed with the National Labor Relations Board ("NLRB") various charges that the Company is engaging in unfair labor practices within the meaning of the National Labor Relations Act ("NLRA"). These charges include allegations that the Company has unlawfully threatened to move its production outside the United States. These allegations have been dismissed by the Regional Director for Region 21 of the NLRB, and the NLRB has rejected UNITE's appeal of the dismissal.

On July 7, 1998, UNITE filed charges against the Company alleging that the Company violated the NLRA by failing to uphold certain obligations under a prior settlement agreement with the NLRB, by denying pro-union employees access to the Company's facilities, by conferring new benefits to employees, by making false accusations against UNITE, by conducting video surveillance of UNITE's offices, and by assisting and organizing an anti-union demonstration. The NLRB has not issued a ruling on these charges. These allegations have been dismissed by the Regional Director for Region 21 of the NLRB.

On February 24, 1998, the Company and Maurice Marciano, Paul Marciano and Armand Marciano, as individuals, were named as defendants in a class action entitled John N. Robinson v. Guess ?, Inc.,

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Maurice Marciano, Paul Marciano and Armand Marciano, Case No. BC186583, filed in the Los Angeles Superior Court. The complaint (the "Complaint") purported to state a claim under Sections 11, 12(a)(2) and 15 of the Securities Act of 1933 for alleged misrepresentations in connection with the Company's initial public offering (the "IPO") in August 1996. Mr. Robinson purported to represent a class of all purchasers of the Company's stock in the IPO and sought unspecified damages.

On October 1, 1998, Mr. Robinson filed an amended complaint ("The Amended Complaint") naming the same parties as defendants. In the Amended Complaint, Mr. Robinson purports to represent the same class of purchasers of the Company's stock in its IPO. As in the original complaint, the Amended Complaint purports to state claims under Sections 11, 12(a)(2) and 15 of the Securities Act of 1933 for alleged misrepresentations in connection with the Company's IPO. On December 15, 1998, the Company filed a Demurrer and Motion to Strike the Amended Complaint. While it is too soon to predict the outcome of the case with any certainty, the Company believes that it has meritorious defenses to each of the claims asserted and intends to vigorously defend itself.

On October 26, 1998, Maurice Marciano, Paul Marciano and Armand Marciano, as individuals, (the "Marcianos"), as well as the Company, were named as defendants

in a shareholder's derivative complaint entitled John N. Robinson v. Maurice Marciano, Paul Marciano and Armand Marciano and Guess?, filed in the Los Angeles Superior Court. The complaint (the "Derivative Complaint") purports to state a claim for intentional breach of fiduciary duty, negligent breach of fiduciary duty, constructive fraud and abuse of control in connection with the Marcianos' management of the Company since its IPO. On January 11, 1999, the Marcianos filed a Demurrer and Motion to Strike the Derivative Complaint. The Company joined in the Demurrer and the Motion to Strike, both of which are set for hearing on March 25, 1999. While it is too soon to predict the outcome of the case with any certainty, the defendants believe they have meritorious defenses to each of the claims asserted and intend to vigorously defend themselves.

The Company believes the outcome of one or more of the above cases could have a material adverse effect on the Company's financial condition and results of operations.

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

- (a) The Registrant's Annual Meeting of Stockholders ("Annual Meeting") was held on May 18, 1998.
- (b) Proxies for the Annual Meeting were solicited pursuant to Regulation 14 under the Securities Exchange Act of 1934, as amended. There was no solicitation in opposition to the management's nominee as listed in the proxy statement. The nominees were elected.
- (c) The results of the matters voted at the Annual Meeting were as follows:
 - (1) To elect the Class II Directors, each to serve as such until the 2001 Annual Meeting of Stockholders and until each of their successors are elected and qualified.

	FOR	AGAINST	ABSTAIN
	-----	-----	-----
Paul Marciano.....	42,363,098	81,625	0
Robert Davis.....	42,358,248	86,475	0

- (2) To ratify the selection of KPMG LLP to serve as independent certified public accountants for the year ended December 31, 1998.

FOR	AGAINST	ABSTAIN
-----	-----	-----
42,407,902	15,440	21,381

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Since August 8, 1996, the Company's Common Stock has been listed on the New York Stock Exchange under the symbol "GES." The following table sets forth, for the periods indicated, the high and low sales prices of the Company's Common Stock, as reported on the New York Stock Exchange Composite Tape.

HIGH LOW

YEAR ENDING DECEMBER 31, 1997

First Quarter 1997.....	14 5/8	10 1/4
Second Quarter 1997.....	13 3/8	10 1/8
Third Quarter 1997.....	10 1/4	8 3/4
Fourth Quarter 1997.....	9 3/4	6 3/8

YEAR ENDING DECEMBER 31, 1998

First Quarter 1998.....	8	5 3/16
Second Quarter 1998.....	7 3/16	4
Third Quarter 1998.....	5	3 3/4
Fourth Quarter 1998.....	7 1/8	3 5/8

YEAR ENDING DECEMBER 31, 1999

First Quarter through February 26, 1999.....	8 1/2	5 1/16
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On February 26, 1999, the closing sales price per share of the Company's Common Stock, as reported on the New York Stock Exchange Composite Tape, was 6 7/8. On February 26, 1999, there were 195 holders of record of the Company's Common Stock.

DIVIDEND POLICY

The Company intends to use its cash flow from operations in 1999 principally to finance the expansion and remodel of its retail stores, shop-in-shop programs and operations. Any future determination as to the payment of dividends will be at the discretion of the Company's Board of Directors and will depend upon the Company's results of operations, financial condition, contractual restrictions and other factors deemed relevant by the Board of Directors. The agreement governing the Company's revolving credit facility and the indenture pursuant to which the Senior Subordinated Notes were issued restrict the payment of dividends by the Company.

Since its IPO on August 8, 1996, the Company has not declared any dividends on its Common Stock.

ITEM 6. SELECTED FINANCIAL DATA

The selected financial data set forth below have been derived from the audited consolidated financial statements of the Company and the related notes thereto. The following selected financial data should be read in conjunction with the Company's consolidated financial statements and the related notes included in Item 14 herein, and Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

	YEAR ENDED DECEMBER 31,				
	1998	1997	1996	1995	1994
	(IN THOUSANDS, EXCEPT PER SHARE DATA)				
STATEMENT OF EARNINGS DATA:					
Net revenue.....	\$ 471,931	\$ 515,372	\$ 551,162	\$ 486,733	\$ 547,812
Earnings from operations.....	57,046	70,646	98,095	82,928	117,807
Net earnings.....	25,111	37,511	66,741	63,919	97,641
SUPPLEMENTAL STATEMENT OF EARNINGS DATA (1)					
Earnings before income taxes and change in accounting principle (2).....	\$ 43,291	\$ 54,887	\$ 82,567	\$ 66,814	\$ 101,181
Income taxes.....	18,180	21,337	33,241	26,726	40,472
Net earnings.....	25,111	37,511	49,326	40,088	60,709
Basic and diluted earnings per share (3).....	\$ 0.59	\$ 0.87	\$ 1.18	\$ 0.96	
Weighted number of shares outstanding -- basic (3)...	42,904	42,898	41,906	41,675	
Weighted number of shares outstanding -- diluted (3).....	42,919	42,902	41,908	41,675	

	DECEMBER 31,				
	1998	1997	1996	1995	1994
BALANCE SHEET DATA:					
Working capital.....	\$ 101,310	\$ 106,670	\$ 76,821	\$ 57,572	\$ 83,127
Total assets.....	263,772	287,814	239,306	202,635	207,696
Notes payable and long-term debt.....	99,000	141,517	127,316	123,335	156,495
Net stockholders' equity.....	100,409	75,330	34,928	10,997	373

(1) Reflects pro forma adjustments for Federal and state income taxes as if the Company had been taxed as a C corporation rather than an S corporation. Prior to the Company's IPO in August 1996, the Company had elected to be taxed as an S corporation for Federal income tax purposes. In certain states, the Company was taxed as an S corporation; in other states, the Company was taxed as a C corporation. Effective January 1, 1991, the Company elected to be treated as an S corporation for

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California tax purposes. As a result of the Company's IPO, all S corporation elections were terminated.

(2) Effective January 1, 1997, the Company changed its method of accounting for product display fixtures located in its wholesale customers' retail stores, whereby the costs for such fixtures are capitalized and amortized over five years using the straight-line method. In prior years, these costs had been expensed as incurred. The Company believes that this new method will more closely match the long-term benefit that the product display fixtures provide with the expected future revenue from such fixtures. The cumulative effect of the change in accounting principle, recorded in the first quarter of 1997, is calculated based upon the retroactive effect of applying the new accounting method to prior year fixture acquisitions. The cumulative effect of the change in accounting principle of \$4.0 million (after reduction for income tax expense of \$2.7 million) is included in earnings for the year ended December 31, 1997. Excluding the cumulative effect of the change in accounting principle, the effect of the change during 1997 was to increase net earnings by approximately \$6.2 million or \$0.14 per share.

(3) 1996 reflects (i) 32,681,819 shares of Common Stock outstanding prior to the IPO and the assumed issuance of 8,730,000 shares of Common Stock at the IPO (\$18.00 per share) to generate sufficient cash to pay a distribution of retained earnings to its then existing stockholders as part of the termination of its S corporation status in an amount equal to retained earnings as of the IPO date and (ii) an average of 42,682,000 shares outstanding subsequent to the IPO, representing the actual shares outstanding. For further information pertaining to the calculation of net earnings per share, see note 1 to the Consolidated Financial Statements.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

GENERAL

The Company derives its net revenue from the sale of Guess men's, women's and girl's apparel worldwide to wholesale customers and distributors, from the sale of Guess men's, women's and girl's apparel and its licensees' products through the Company's network of retail and factory outlet stores primarily in the United States and from net royalties from worldwide licensing activities.

ACTUAL AND PRO FORMA RESULTS OF OPERATIONS

The following table sets forth actual operating results for the 1998 and 1997 periods and pro forma operating results for the 1996 period. Pro forma operating results reflect adjustments to the 1996 historical operating results for (i) the elimination of salaries and bonuses paid to Maurice, Paul and Armand Marciano ("Principal Executive Officers") in excess of an aggregate of \$4.9 million per year (the estimated aggregate salaries and bonuses to be paid to the

Principal Executive Officers under their respective employment agreements which became effective concurrently with the consummation of the IPO), resulting in a decrease in compensation expense of \$3.5 million; (ii) the decrease in depreciation and operating costs of \$1.2 million, associated with an aircraft owned by the Company, which was sold in contemplation of the IPO; (iii) the elimination of the minority interest in Guess Europe, B.V. ("GEBV") and Guess? Italia, S.r.l. ("Guess? Italia") through the merger of Marciano International, Inc. ("Marciano International") with and into the Company in connection with the IPO, resulting in the inclusion in net earnings of \$323,000, which amounts had previously been recorded as minority interest; and

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(iv) adjustments for Federal and state income taxes as if the Company had been taxed as a C corporation rather than an S corporation throughout the periods presented.

	YEAR ENDED DECEMBER 31,		
	1998	1997	1996
	(IN THOUSANDS) (PRO FORMA)		
Net revenue:			
Product sales.....	\$ 435,128	\$ 465,913	\$ 497,874
Net royalties.....	36,803	49,459	53,288
Total net revenue.....	471,931	515,372	551,162
Cost of sales.....	272,079	288,408	298,631
Gross profit.....	199,852	226,964	252,531
Selling, general and administrative expenses.....	142,806	156,318	146,186
Earnings from operations before reorganization charge.....	57,046	70,646	106,345
Reorganization charge.....	--	--	3,559
Earnings from operations.....	57,046	70,646	102,786
Other income (expense):			
Interest expense, net.....	(12,892)	(13,718)	(14,539)
Other income (expense), net.....	(863)	(2,041)	(666)
Earnings before income taxes and cumulative effect of change in accounting principle.....	(13,755)	(15,759)	(15,205)
Income taxes.....	43,291	54,887	87,581
Earnings before cumulative effect of change in accounting principle.....	18,180	21,337	35,257
Cumulative effect of change in accounting for product display fixtures, net of income taxes of \$2,707.....	25,111	33,550	52,324
Net earnings.....	--	3,961	--
Net earnings.....	\$ 25,111	\$ 37,511	\$ 52,324

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The following table sets forth actual operating results for the 1998 and 1997 periods and pro forma operating results for the 1996 period as a percentage of net revenue.

	YEAR ENDED DECEMBER 31,		
	1998	1997	1996
	(PRO FORMA)		
Net revenue:			
Product sales.....	92.2%	90.4%	90.3%
Net royalties.....	7.8	9.6	9.7
Total net revenue.....	100.0	100.0	100.0
Cost of sales.....	57.7	56.0	54.2
Gross profit.....	42.3	44.0	45.8
Selling, general and administrative expenses.....	30.3	30.3	26.5
Earnings from operations before reorganization charge.....	12.1	13.7	19.3
Reorganization charge.....	--	--	0.7
Earnings from operations.....	12.1	13.7	18.6
Other income (expense):			
Interest expense, net.....	(2.7)	(2.7)	(2.6)

Other income (expense), net.....	(0.2)	(0.4)	(0.1)
	-----	-----	-----
Earnings before income taxes and cumulative effect of change in accounting principle.....	(2.9)	(3.1)	(2.7)
Income taxes.....	9.2	10.6	15.9
	-----	-----	-----
	3.9	4.1	6.4
Earnings before cumulative effect of change in accounting principle.....	5.3	6.5	9.5
Cumulative effect of change in accounting for product display fixtures, net of income taxes of \$2,707).....	--	0.8	--
	-----	-----	-----
Net earnings.....	5.3%	7.3%	9.5%
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YEAR ENDED DECEMBER 31, 1998 COMPARED TO YEAR ENDED DECEMBER 31, 1997.

NET REVENUE. Net revenue decreased \$43.5 million or 8.4% to \$471.9 million in the year ended December 31, 1998 from \$515.4 million in the year ended December 31, 1997. Net revenue from wholesale operations decreased \$37.5 million or 15.0% to \$212.5 million from \$250.0 million. Domestic and international wholesale operations net revenue decreased by \$18.2 million and \$19.3 million, respectively. The Company's domestic wholesale net revenue declined primarily as a result of increased competition in branded basic denim apparel. International wholesale operations decreased due primarily to the sale of the Guess? Italia wholesale operations in June 1997, which had contributed \$13.5 million during the first five months of the prior year, as well as soft performance in Asian and South American markets. Net revenue from retail operations increased \$6.7 million or 3.1% to \$222.6 million from \$215.9 million, from volume generated by new store openings, partially offset by a 5.6% decrease in comparable store net revenue. The decrease in comparable store net revenue was primarily due to product assortment changes in the Company's outlet stores and softening Pacific Rim tourism, which significantly impacted West Coast business during the first half of the year. During the second half of the year, full-priced stores experienced positive comparable store net revenue, primarily due to improved merchandising and store operational initiatives implemented by a new retail management team. Net royalties decreased \$12.7 million or 25.6% in the year ended December 31, 1998 to \$36.8 million from \$49.5 million in the year ended December 31, 1997. The decline in net royalties was primarily the result of the termination of various under-performing licenses, discontinuation of certain licenses that were brought back in-house, continuing economic turmoil

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and currency devaluation in Asian markets and the financial difficulty of a domestic licensee. Net revenue from international operations comprised 8.0% and 11.5% of the Company's net revenue during 1998 and 1997, respectively.

GROSS PROFIT. Gross profit decreased 11.9% to \$199.9 million in the year ended December 31, 1998 from \$227.0 million in the year ended December 31, 1997. The decline in gross profit resulted from lower net royalties, as well as decreased net revenue from product sales. Gross profit from product sales decreased 8.1% to \$163.0 million in the year ended December 31, 1998 from \$177.5 million in the year ended December 31, 1997. Gross margin decreased to 42.3% in the year ended December 31, 1998 as compared to 44.0% in the year ended December 31, 1997. Gross margin from product sales decreased to 37.5% in the year ended December 31, 1998 compared to 38.1% in the year ended December 31, 1997. The decrease in gross margin from product sales was primarily the result of fixed store occupancy costs being spread over a lower comparable store revenue base, partially offset by a favorable mix in retail net revenue (which generally carries a higher gross margin rate) and lower wholesale markdowns and allowances.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative ("SG&A") expenses decreased 8.6% in the year ended December 31, 1998 to \$142.8 million, or 30.3% of net revenue, from \$156.3 million, or 30.3% of net revenue, in the year ended December 31, 1997. The dollar decrease in SG&A expenses was primarily due to cost reduction initiatives implemented in the fourth quarter of 1997.

EARNINGS FROM OPERATIONS. Earnings from operations decreased 19.3% to \$57.0 million, or 12.1% of net revenue, for the year ended December 31, 1998 from

\$70.6 million, or 13.7% of net revenue, for the year ended December 31, 1997. The decrease in earnings from operations was primarily due to lower revenue.

INTEREST EXPENSE, NET. Net interest expense decreased 6.0% to \$12.9 million in the year ended December 31, 1998 from \$13.7 million in the year ended December 31, 1997. This decrease resulted primarily from lower outstanding average debt, partially offset by a slightly higher average effective interest rate. For the year ended December 31, 1998, the average debt balance was \$135.5 million, with an average effective interest rate of 9.0%. For the year ended December 31, 1997, the average debt balance was \$148.4 million, with an average effective interest rate of 8.8%.

OTHER EXPENSES. Other non-operating expenses were \$0.9 million in the year ended December 31, 1998 as compared to \$2.0 million in the year ended December 31, 1997. The decrease was primarily due to a \$1.4 million write-down to the lower of cost or market of an equity investment during 1997.

INCOME TAXES. The income tax provision for the year ended December 31, 1998 was \$18.2 million, or a 42.0% effective tax rate. The income tax provision for the year ended December 31, 1997 was \$21.3 million, or a 38.9% effective tax rate. The effective tax rate for 1998 was adversely impacted primarily by Federal and state income taxes related to a dividend declared to the Company by one of the its foreign subsidiaries.

NET EARNINGS BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE. Net earnings before the net cumulative effect of a change in accounting principle decreased by 25.2% to \$25.1 million, or 5.3% of net revenue, in the year ended December 31, 1998 from \$33.5 million, or 6.5% of net revenue, in the year ended December 31, 1997.

NET EARNINGS. Net earnings decreased to \$25.1 million in the year ended December 31, 1998, from \$37.5 million in the year ended December 31, 1997.

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YEAR ENDED DECEMBER 31, 1997 COMPARED TO YEAR ENDED DECEMBER 31, 1996.

NET REVENUE. Net revenue decreased \$35.8 million or 6.5% to \$515.4 million in the year ended December 31, 1997 from \$551.2 million in the year ended December 31, 1996. Net revenue from wholesale operations decreased \$38.1 million or 13.2% to \$250.0 million from \$288.1 million. Domestic and international wholesale operations net revenue decreased by \$26.1 million and \$12.0 million, respectively. The Company's domestic wholesale net sales declined primarily as a result of increased competition in branded basic denim apparel and \$10.0 million in markdowns and returns in excess of anticipated levels in the 1997 period. International wholesale operations decreased primarily due to the sale of the Guess? Italia operations during the second quarter of 1997. Net revenue from retail operations increased \$6.1 million or 2.9% to \$215.9 million from \$209.8 million, from volume generated by new store openings, partially offset by an 8.4% decrease in comparable store net revenue. The decrease in comparable store revenue was primarily due to production delays related to fabric and a loss of merchandise in a factory fire during the first half of 1997, as well as softening Pacific Rim tourism adversely affecting west coast stores and aggressive campaigns against the Company by UNITE (see also "Legal Proceedings"). Net royalties decreased 7.1% in the year ended December 31, 1997 to \$49.5 million from \$53.3 million in the year ended December 31, 1996. The decline in net royalties was primarily due to lower royalties resulting from discontinued licenses and non-recurring technical assistance fees recorded in the second quarter of 1996, partially offset by the increase in net royalties from new licensees. Net revenue from international operations comprised 11.5% and 12.1% of the Company's net revenue during 1997 and 1996, respectively.

GROSS PROFIT. Gross profit decreased 10.1% to \$227.0 million in the year ended December 31, 1997 from \$252.5 million in the year ended December 31, 1996. The decline in gross profit resulted from lower net royalties, as well as decreased net revenue from product sales. Gross profit from product sales decreased 10.9% to \$177.5 million in the year ended December 31, 1997 from \$199.2 million in the year ended December 31, 1996. Gross margin decreased to

44.0% in the year ended December 31, 1997 as compared to 45.8% in the year ended December 31, 1996. Gross margin from product sales decreased to 38.1% in the year ended December 31, 1997 compared to 40.0% in the year ended December 31, 1996. The decline in the gross margin was primarily the result of higher domestic wholesale markdowns and fixed store occupancy costs being spread over a lower revenue base in the 1997 period.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. SG&A expenses increased 3.6% in the year ended December 31, 1997 to \$156.3 million, or 30.3% of net revenue, from \$150.9 million, or 27.4% of net revenue, in the year ended December 31, 1996. On a pro forma basis, SG&A expenses would have increased 6.9% in the year ended December 31, 1997 to \$156.3 million, or 30.3% of net revenue, from \$146.3 million, or 26.5% of net revenue, in the year ended December 31, 1996. The increase in SG&A expense was primarily the result of higher depreciation expense associated with increased capital expenditures, higher legal costs associated with UNITE activities (see "Legal Proceedings"), \$3.1 million in non-recurring general and administrative expenses and increased store expenses related to the expansion of the retail operations.

REORGANIZATION CHARGE. In anticipation of the IPO, in the second quarter of 1996, the Company recorded reserves for certain non-recurring charges related to the write-downs of operating assets to be disposed amounting to \$3.6 million for (i) disposal of two remote warehouse and production facilities resulting in a net book loss of \$2.4 million, and (ii) the net book loss of \$1.2 million incurred by the Company in connection with the sale of one of its aircraft. The above charges were based upon the book value of the related assets as of June 30, 1996. The Company intends to relocate the warehouse and production operations located at the remote facilities to its central facility in Los Angeles in an effort to centralize its operations and improve operating efficiencies.

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INTEREST EXPENSE, NET. Net interest expense decreased 5.6% to \$13.7 million in the year ended December 31, 1997 from \$14.5 million in the year ended December 31, 1996. This decrease resulted primarily from a lower average effective interest rate, partially offset by slightly higher outstanding average debt. For the year ended December 31, 1997, the average debt balance was \$148.4 million, with an average effective interest rate of 8.8%. For the year ended December 31, 1996, the average debt balance was \$144.4 million, with an average effective interest rate of 9.4%.

OTHER EXPENSES. Other non-operating expenses were \$2.0 million in the year ended December 31, 1997 as compared to \$1.0 million in the year ended December 31, 1996. On a pro forma basis, other non-operating expenses would have been \$2.0 million in the year ended December 31, 1997 compared to \$0.7 million in the year ended December 31, 1996. The increase was primarily due to a \$1.4 million write-down to the lower of cost or market of an equity investment.

INCOME TAXES. Prior to the IPO, for Federal and certain state income tax purposes, the Company elected to be treated as an S corporation and therefore generally was not subject to income tax on its earnings. The Company's income taxes, which represent state and foreign income taxes, plus Federal income taxes after the IPO, were \$21.3 million and \$15.8 million in the years ended December 31, 1997 and December 31, 1996, respectively. The Company's S corporation status was terminated in connection with the IPO and, therefore, the Company is now fully subject to Federal, state and foreign income taxes. On a pro forma basis, income taxes would have been \$21.3 million and \$35.3 million in the years ended December 31, 1997 and December 31, 1996, respectively.

NET CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE. Effective January 1, 1997, the Company changed its method of accounting for product display fixtures located in its wholesale customers' retail stores, whereby the costs for such fixtures will be capitalized and amortized over five years using the straight-line method. In prior years, these costs were expensed as incurred. The Company believes this new method will more closely match the long-term benefit the product display fixtures provide with the expected future revenue from such fixtures. The cumulative effect of the change in accounting principle, recorded

in the first quarter of 1997, is calculated based on the retroactive effect of applying the new accounting method to prior year fixture acquisitions. The cumulative effect of the change in accounting principle of \$4.0 million (after reduction for income tax expense of \$2.7 million) is included in earnings for the year ended December 31, 1997. Excluding the cumulative effect of the change in accounting principle, the effect of the change during 1997 was to increase net earnings by approximately \$6.2 million or \$0.14 per share.

NET EARNINGS. Net earnings decreased to \$37.5 million in the year ended December 31, 1997, from \$66.7 million in the year ended December 31, 1996. On a pro forma basis, net earnings would have decreased to \$37.5 million in the year ended December 31, 1997, from \$52.3 million in the year ended December 31, 1996. Excluding the cumulative effect of the change in accounting principle in 1997 and reorganization charge in 1996, pro forma net earnings would have decreased by 35.9% to \$33.5 million, or 6.5% of net revenue, in the year ended December 31, 1997 from \$54.4 million, or 9.9% of net revenue, in the year ended December 31, 1996.

LIQUIDITY AND CAPITAL RESOURCES

The Company has relied primarily upon internally generated funds, trade credit and bank borrowings to finance its operations. At December 31, 1998 the Company had working capital of \$101.3 million, compared to \$106.7 million at December 31, 1997. The \$5.4 million decrease in working capital is primarily due to a \$14.9 million decrease in prepaid taxes and other current assets, a \$3.6 million decrease in net receivables, and a \$2.6 million decrease in inventory, partially offset by a net \$9.5 million increase in cash and short-term investments and a \$5.5 million decrease in accounts payable.

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The Company's Credit Agreement, as amended, provides for a \$100.0 million revolving credit facility, which includes a \$25.0 million sublimit for letters of credit. At December 31, 1998, the Company had no outstanding borrowings under the revolving credit facility, \$1.7 million in outstanding standby letters of credit and \$11.3 million in outstanding commercial letters of credit. At December 31, 1998, the Company had \$87.0 million available for future borrowings under such facility. The revolving credit facility will expire in December 1999. The Credit Agreement contains various restrictive covenants requiring, among other things, the maintenance of certain financial ratios. The Company was in compliance with all such covenants as of December 31, 1998.

Capital expenditures, net of lease incentives granted, totaled \$13.3 million for 1998 and \$46.3 million for 1997. The decrease in capital expenditures was due primarily to fewer store openings and lower expenditures for shop-in-shop programs. The Company estimates that its capital expenditures for 1999 will be approximately \$22.0 million, primarily for retail store expansion and remodeling, the shop-in-shop program and operations.

The Company anticipates it will be able to satisfy its ongoing cash requirements through 1999, including retail expansion plans and interest payments on the Company's Senior Subordinated Notes, primarily with cash flow from operations, supplemented, if necessary, by borrowings under its revolving Credit Agreement and anticipated replacements thereof.

OTHER MATTERS

YEAR 2000 ISSUE

The Year 2000 issue is primarily a result of older computer programs, commercial systems, and embedded chips, using a two-digit format, as opposed to a four-digit format, to indicate the year. The business risk is that some of these systems might be unable to interpret dates beyond 1999. Such a failure might cause a disruption to the operations of the system(s) and/or the business function(s) it supports.

In recognition of this risk, the Company has established a Year 2000 Project Team. The Company began its Year 2000 readiness assessment and remediation

efforts in 1996. The effort was divided into 4 phases: Phase 1: assessment, Phase 2: remediation, Phase 3: testing and certification and Phase 4: contingency plans.

STATE OF READINESS

Phase 1 and Phase 2 included a review of all hardware and software systems, business functions and trading partners that contain and/or exchange date-sensitive information. Critical IT systems, which include its enterprise-wide information system, time clocks, e-mail and phone systems, are stated Year 2000 compliant with initial testing of systems currently underway. The Company is currently performing diagnostics and implementing Year 2000 compliant solutions in its non-IT systems, such as manufacturing equipment and those systems involved with facility management (security systems, air/heating systems, fire suppression systems). Phases 1 and 2 are concluded. The Company estimates that it will complete its Phase 3 Testing and Certification efforts by mid-1999.

The Company's Year 2000 Project Team is coordinating the global effort and monitoring progress of the Year 2000 readiness with respect to its business partners. The Company has initiated communications with all of its key business partners to determine their extent and plans for Year 2000 compliance. As part of this process, the Company has requested written assurances from its key external business partners as to their Year 2000 readiness status and their plans to become Year 2000 compliant when necessary. As of December 31, 1998, the Company has received responses from most of its key vendors acknowledging their compliance, or intent to comply, with Year 2000 issues. In the case of some key vendors, the Company has, and will continue to, obtain and review the compliance testing plans and results to validate the assurances. This process is ongoing and is expected to continue throughout 1999.

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RISKS AND CONTINGENCY PLANS OF YEAR 2000 ISSUES

The Company has begun the development of its BUSINESS CONTINUITY PLAN. The initial phases of the plan are expected to be completed by mid-year 1999. The timing of a Year 2000 related disruption would coincide with a seasonal low in the Company's business cycle, therefore having less impact on the business.

The Company believes that the reasonably likely worst case scenario would involve a short-term disruption of systems affecting its supply and distribution channels. These risks include: a) delayed product deliveries from suppliers, b) disruption to the distribution channel, including ports, transportation vendors, government agencies, as well as the Company's own facilities, and c) general isolated failures of systems and necessary infrastructure such as electric, water, or communications supply.

At the present time, the Company is not aware of any Year 2000 issues that are expected to affect materially its products, services, competitive position or financial performance. However, despite the significant and best-efforts to make its systems and facilities Year 2000 compliant, the compliance of its business partners and third-party service providers, is beyond the Company's control. Accordingly, the Company can give no assurances that the failure of key suppliers or other third parties to comply with Year 2000 requirements will not have an adverse effect on the Company.

COSTS TO ADDRESS YEAR 2000 ISSUES

The costs to plan for, modify, or replace systems for the Year 2000 problem are estimated by the Company to amount to approximately \$3 million. The costs associated with the Year 2000 project have been budgeted and tracked as a separate project and have been occurring in conjunction with normal operating activities. These costs are being funded through operating cash flows and being expensed over the four-year project period, as incurred. The Company has engaged and will continue to engage external expertise to supplement internal staff. Management believes that the internal staff time invested to address Year 2000 issues should not have a materially adverse affect on other projects and is, in

fact, effecting process improvements as a by-product of this investment.

LABOR ISSUES

The Union of Needletrades, Industrial and Textile Employees ("UNITE") has continued to conduct a corporate campaign against the Company. In addition to the legal proceedings (See "Legal Proceedings") initiated by UNITE, UNITE has, and continues to, through the media and other means attempted to tarnish the Company's image and affect the sales of the Company's product. The Company believes that such corporate campaign could have a material adverse effect on the Company's financial condition and results of operations.

IMPORTANT FACTORS REGARDING FORWARD-LOOKING STATEMENTS

Various forward-looking statements have been made in this Form 10-K. Forward-looking statements may also be in the registrant's other reports filed under the Securities Exchange Act of 1934, in its press releases and in other documents. In addition, from time to time, the registrant through its management may make oral forward-looking statements.

Forward-looking statements generally refer to future plans and performance, and are identified by the words "believe," "expect," "anticipate," "optimistic," "intend," "aim," "will" or similar expressions. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of which they are made. The registrant undertakes no obligation to update publicly or revise any forward-looking statements.

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Important factors that could cause actual results to differ materially from the registrant's forward-looking statements, as well as affect the registrant's ability to achieve its financial and other goals, include, but are not limited to, the following:

- The Company's inability to identify and respond appropriately to changing consumer demands and fashion trends could adversely affect consumer acceptance of Guess products.
- A decision by the controlling owner of a group of department stores or any other significant customer to decrease the amount purchased from the Company or to cease carrying Guess products could have a material adverse effect on the Company's financial condition and results of operations.
- The inability of the Company to control the quality, focus, image, financial stability or distribution of its licensed products could impact consumer receptivity to the Company's products generally and, therefore, adversely affect the Company's financial condition and results of operations.
- The failure of the Company to continue to enhance operating control systems could adversely affect the Company's financial condition and results of operations.
- Factors beyond the Company's control may affect the Company's ability to expand its network of retail stores including the unavailability of acceptable store locations and general economic and business conditions affecting consumer spending.
- A general failure by the Company to maintain and control its existing distribution and licensing arrangements or to procure additional distribution and licensing relationships could adversely affect the Company's growth strategy, which could adversely affect the Company's financial condition and results of operations.
- The extended loss of the services of one or more of the Principal Executive Officers could have a material adverse effect on the Company's operations.

- The Company's operations may be affected adversely by political instability resulting in the disruption of trade with the countries in which the Company's contractors, suppliers or customers are located, the imposition of additional regulations relating to imports, the imposition of additional duties, taxes and other charges on imports, significant fluctuations in the value of the dollar against foreign currencies or restrictions on the transfer of funds. Also, a substantial increase in customs duties could have an adverse effect on the Company's financial condition or results of operations. These factors may be exacerbated by the Company's increasing use of packaged purchase sourcing from non-United States vendors.
- The inability of a manufacturer to ship the Company's products in a timely manner or to meet the Company's quality standards could adversely affect the Company's ability to deliver products to its customers in a timely manner.
- No assurance can be given that others will not assert rights in, or ownership of, trademarks and other proprietary rights of Guess. In addition, the laws of certain foreign countries do not protect proprietary rights to the same extent as do the laws of the United States.

SEASONALITY

The Company's business is impacted by general seasonal trends characteristic of the apparel and retail industries. The Company's wholesale operations generally experience stronger performance in the first and third quarters, while retail operations are generally stronger in the third and fourth quarters. As the timing of the shipment of products may vary from year to year, the result for any particular quarter may not be indicative of results for the full year. The Company has not had significant overhead and other costs generally associated with large seasonal variations.

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INFLATION

The Company does not believe the relatively moderate rates of inflation experienced in the United States over the last three years have had a significant effect on its net revenue or profitability. Although higher rates of inflation have been experienced in a number of foreign countries in which the Company's products are manufactured, the Company does not believe they have had a material effect on the Company's net revenue or profitability.

EXCHANGE RATES

The Company receives United States dollars for substantially all of its product sales and its licensing revenues. Inventory purchases from offshore contract manufacturers are primarily denominated in United States dollars; however, purchase prices for the Company's products may be impacted by fluctuations in the exchange rate between the United States dollar and the local currencies of the contract manufacturers, which may have the effect of increasing the Company's cost of goods in the future. In addition, royalties received from the Company's international licensees are subject to foreign currency translation fluctuations as a result of the net sales of the licensee being denominated in local currency and royalties being paid to the Company in United States dollars. During the last three fiscal years, exchange rate fluctuations have not had a material impact on the Company's inventory costs. The Company currently does not engage in hedging activities with respect to such exchange rate risk.

IMPACT OF RECENT ACCOUNTING PRONOUNCEMENTS

In March 1998, the American Institute of Certified Public Accountants issued Statement of Position 98-5, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use" ("SOP 98-5"). SOP 98-5 provides guidance on accounting for the costs of computer software developed or obtained for internal use. It is effective for fiscal years beginning after December 15,

1998. The Company intends to adopt SOP 98-5 during the fiscal year ended December 31, 1999. The Company has determined that the adoption of SOP 98-5 will not have a material impact on the Company's financial reporting.

In April 1998, the AICPA Accounting Standards Executive Committee issued Statement of Position 98-1 ("SOP 98-1"), "Reporting on the Costs of Start-up Activities." SOP 98-1 requires that costs of start-up activities, including organization costs and retail store openings, be expensed as incurred. SOP 98-1 is effective for financial statements for fiscal years beginning after December 15, 1998. Earlier application is encouraged. Restatement of previously issued financial statements is not permitted. In the fiscal year in which the SOP 98-1 is first adopted, the application should be reported as a cumulative effect of a change in accounting principle. Management believes the adoption of SOP 98-1 will not have a material impact on the Company's financial reporting.

In June 1998, Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133") was issued. SFAS 133 establishes accounting and reporting standards for derivative instruments and for hedging activities. It is effective for all fiscal quarters of fiscal years beginning after June 15, 1999. The Company currently does not have any derivative financial instruments and does not currently employ any hedging activities.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

Not applicable.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The information required by this Item is incorporated herein by reference to the Financial Statements and Supplementary Data listed in Item 14 of Part IV of this report.

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ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS

Information with respect to Directors may be found under the caption "Directors and Executive Officers" in the Company's Proxy Statement ("Proxy Statement") dated March 31, 1999, for the 1999 Annual Meeting of Shareholders to be held May 17, 1999. Such information is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION AND OTHER INFORMATION

The information in the Proxy Statement set forth under the caption "Executive Compensation" is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information set forth under the caption "Security Ownership and Certain Beneficial Owners and Management" in the Company's Proxy Statement is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information set forth under the caption "Certain Relationships and Related Transactions" in the Company's Proxy Statement is incorporated herein by reference.

PART IV

ITEM 14. EXHIBITS, CONSOLIDATED FINANCIAL STATEMENT SCHEDULE, AND REPORTS ON FORM 8-K

(a) Documents Filed with Report

(1) Consolidated Financial Statements

The financial statements listed on the accompanying Index to Consolidated Financial Statements and Financial Statement Schedule are filed as part of this report.

(2) Consolidated Financial Statement Schedule

The financial statement schedule listed on the accompanying Index to Consolidated Financial Statements and Financial Statement Schedule are filed as part of this report.

(3) Exhibits

The exhibits listed on the accompanying Index to Exhibits are filed as part of this report.

(b) Reports on Form 8-K

No reports on Form 8-K were filed by the Company during the last quarter of the fiscal year ended December 31, 1998.

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GUESS ?, INC.

FORM 10-K

ITEMS 8, 14(A) AND 14(D)

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND FINANCIAL STATEMENT SCHEDULE

1	Consolidated Financial Statements	
	Independent Auditors' Report.....	F-2
	Consolidated Balance Sheets at December 31, 1998 and 1997.....	F-3
	Consolidated Statements of Earnings for the Years Ended December 31, 1998, 1997 and 1996	F-4
	Consolidated Statements of Stockholders' Equity and Comprehensive Income (Loss) for the Years Ended December 31, 1998, 1997 and 1996.....	F-5
	Consolidated Statements of Cash Flows for the Years Ended December 31, 1998, 1997 and 1996.....	F-6
	Notes to Consolidated Financial Statements.....	F-7
2	Consolidated Financial Statement Schedule Valuation and Qualifying Accounts.....	F-27

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INDEPENDENT AUDITORS' REPORT

The Board of Directors and Stockholders
Guess ?, Inc.:

We have audited the accompanying consolidated financial statements of Guess ?, Inc. and Subsidiaries as listed in the accompanying index. In connection with our audits of the consolidated financial statements, we also have audited the consolidated financial statement schedule, as listed in the accompanying index. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Guess ?, Inc. and Subsidiaries at December 31, 1998 and 1997 and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 1998 in conformity with generally accepted accounting principles. Also in our opinion, the related consolidated financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

As discussed in note 16, the Company changed its method of accounting for its product display fixtures in 1997.

KPMG LLP

Los Angeles, California
February 17, 1999

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GUESS ?, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

DECEMBER 31, 1998 AND 1997

(IN THOUSANDS, EXCEPT SHARE DATA)

ASSETS	1998	1997
	-----	-----
Current assets:		
Cash.....	\$ 5,853	\$ 8,204
Investments (note 2).....	11,900	--
Receivables:		
Trade receivables, less reserves aggregating \$7,837 and \$11,196 at December 31, 1998 and 1997, respectively.....	19,685	17,080
Royalties, less allowance for doubtful accounts of \$3,667 and \$0 at December 31, 1998 and 1997, respectively.....	10,780	14,663
Other.....	3,673	6,032
	-----	-----
Inventories (note 3).....	34,138	37,775
Prepaid expenses.....	89,499	92,081
Prepaid taxes.....	5,640	5,422
Deferred tax assets (note 6).....	2,566	14,705
	6,496	9,435
	-----	-----
Total current assets.....	156,092	167,622
Property and equipment, at cost, net of accumulated depreciation and amortization (note 4).....	86,453	98,170
Investments (note 2).....	1,118	2,340
Other assets, at cost, net of accumulated amortization of \$2,293 and \$790 at December 31, 1998 and 1997, respectively (notes 6 and 14).....	20,109	19,682
	-----	-----
	\$ 263,772	\$ 287,814
	-----	-----
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current installments of notes payable and long-term debt (note 5).....	\$ --	\$ 217
Accounts payable.....	32,802	38,323

Accrued expenses.....	21,770	22,314
Income taxes payable (note 6).....	210	98
	-----	-----
Total current liabilities.....	54,782	60,952
Notes payable and long-term debt, excluding current installments (note 5).....	99,000	141,300
Other liabilities.....	9,581	10,232
	-----	-----
	163,363	212,484
Stockholders' equity (note 7):		
Preferred stock, \$0.01 par value. Authorized 10,000,000 shares; no shares issued and outstanding.....	--	--
Common stock, \$0.01 par value. Authorized 150,000,000 shares; issued 62,637,327 and 62,928,827 shares at 1998 and 1997, outstanding 42,906,535 and 42,898,035 shares actual, respectively.....	137	137
Paid-in capital.....	158,589	158,589
Retained earnings.....	92,543	67,432
Accumulated other comprehensive income (loss).....	(84)	(52)
Treasury stock, 20,030,792 shares repurchased.....	(150,776)	(150,776)
	-----	-----
Net stockholders' equity.....	100,409	75,330
Commitments and contingencies (note 9).....		
	-----	-----
	\$ 263,772	\$ 287,814
	-----	-----

See accompanying notes to consolidated financial statements

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GUESS ?, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS

YEARS ENDED DECEMBER 31, 1998, 1997 AND 1996

(IN THOUSANDS, EXCEPT PER SHARE DATA)

	1998	1997	1996
	-----	-----	-----
Net revenue			
Product sales.....	\$ 435,128	\$ 465,913	\$ 497,874
Net royalties.....	36,803	49,459	53,288
	-----	-----	-----
	471,931	515,372	551,162
Cost of sales.....	272,079	288,408	298,631
	-----	-----	-----
Gross profit.....	199,852	226,964	252,531
Selling, general and administrative expenses.....	142,806	156,318	150,877
Reorganization charge (note 15).....	--	--	3,559
	-----	-----	-----
Earnings from operations.....	57,046	70,646	98,095
Other income/(expense):			
Interest, net.....	(12,892)	(13,718)	(14,539)
Other, net.....	(863)	(2,041)	(989)
	-----	-----	-----
	(13,755)	(15,759)	(15,528)
Earnings before income taxes and cumulative effect of change in accounting principle.....	43,291	54,887	82,567
Income taxes (note 6).....	18,180	21,337	15,826
	-----	-----	-----
Earnings before cumulative effect of change in accounting principle.....	25,111	33,550	66,741
Cumulative effect of change in accounting for product display fixtures, net of income taxes of \$2,707 (note 16).....	--	3,961	--
	-----	-----	-----
Net earnings.....	\$ 25,111	\$ 37,511	\$ 66,741
	-----	-----	-----
SUPPLEMENTAL PRO FORMA FINANCIAL INFORMATION (NOTE 1):			
Earnings before income taxes and cumulative effect of change in accounting principle, as presented.....	\$ 43,291	\$ 54,887	\$ 82,567
Income taxes (1996 period, pro forma) (unaudited) (note 6).....	18,180	21,337	33,241
	-----	-----	-----
Earnings before cumulative effect of change in accounting principle (1996 period, pro forma) (unaudited).....	25,111	33,550	49,326
Cumulative effect of change in accounting for product display fixtures, net of income taxes of \$2,707 (note 16).....	--	3,961	--
	-----	-----	-----
Net earnings (1996 period, pro forma) (unaudited) (note 6).....	\$ 25,111	\$ 37,511	\$ 49,326
	-----	-----	-----
BASIC AND DILUTED EARNINGS PER SHARE:			
Earnings before cumulative effect of change in accounting principle (1996			

period pro forma).....	\$ 0.59	\$ 0.78	\$ 1.18
Cumulative effect of change in accounting for product display fixtures, net of income taxes of \$2,707 (note 16).....	--	0.09	--
Net earnings (1996 period pro forma).....	\$ 0.59	\$ 0.87	\$ 1.18
Weighted number of shares outstanding--basic.....	42,904	42,898	41,906
Weighted number of shares outstanding--diluted.....	42,919	42,902	41,908

See accompanying notes to consolidated financial statements

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GUESS ?, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
AND COMPREHENSIVE INCOME/(LOSS)

YEARS ENDED DECEMBER 31, 1998, 1997 AND 1996

	COMPREHENSIVE INCOME	COMMON STOCK	PAID-IN CAPITAL	RETAINED EARNINGS	ACCUMULATED OTHER COMPREHENSIVE INCOME	TREASURY STOCK	TOTAL
	(IN THOUSANDS)						
Balance at December 31, 1995.....		\$ 35	\$ 181	\$ 161,567	\$ (10)	\$ (150,776)	\$ 10,997
Comprehensive income:							
Net earnings.....	\$ 66,741	--	--	66,741	--	--	66,741
Foreign currency translation adjustment.....	67	--	--	--	67	--	67
Total comprehensive income.....	\$ 66,808	35	181	228,308	57	(150,776)	77,805
Stockholder distributions.....		--	--	(224,600)	--	--	(224,600)
Issuance of common stock.....		100	169,200	--	--	--	169,300
Reclassification of Stockholder distributions in excess of retained earnings.....		--	(15,252)	15,252	--	--	--
Net equity adjustments resulting from Marciano International merger.....		--	1,462	10,961	--	--	12,423
Balance at December 31, 1996.....		135	155,591	29,921	57	(150,776)	34,928
Comprehensive income:							
Net earnings.....	\$ 37,511	--	--	37,511	--	--	37,511
Foreign currency translation adjustment.....	(109)	--	--	--	(109)	--	(109)
Total comprehensive income.....	\$ 37,402						
Issuance of common stock.....		2	2,998	--	--	--	3,000
Balance at December 31, 1997.....		137	158,589	67,432	(52)	(150,776)	75,330
Comprehensive income:							
Net earnings.....	\$ 25,111	--	--	25,111	--	--	25,111
Foreign currency translation adjustment.....	(32)	--	--	--	(32)	--	(32)
Total comprehensive income.....	\$ 25,079						
Balance at December 31, 1998.....		\$ 137	\$ 158,589	\$ 92,543	\$ (84)	\$ (150,776)	\$ 100,409

See accompanying notes to consolidated financial statements

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GUESS ?, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 1998, 1997 AND 1996

(IN THOUSANDS)

	1998	1997	1996
Cash flows from operating activities:			

Net earnings.....	\$ 25,111	\$ 37,511	\$ 66,741
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Depreciation and amortization of property and equipment.....	22,571	20,071	16,233
Amortization of other assets.....	931	369	804
Amortization of deferred royalty income.....	--	(2,623)	--
Cumulative effect of change in accounting principle.....	--	(3,961)	--
Loss on disposition of property and equipment.....	1,483	120	2,235
Foreign currency translation adjustment.....	(89)	91	42
Contributions from minority interest.....	--	--	336
Equity method losses.....	87	603	666
(Increase) decrease in:			
Receivables.....	3,637	8,988	(8,811)
Inventories.....	2,582	(12,591)	(6,529)
Prepays and other current assets.....	2,719	(3,189)	(1,941)
Prepaid taxes.....	12,141	(14,511)	(8)
Other assets.....	(324)	8,105	(411)
Increase (decrease) in:			
Accounts payable.....	(5,520)	(964)	(1,447)
Accrued expenses.....	(241)	(993)	6,058
Income taxes payable.....	112	(6,784)	2,867
Net cash provided by operating activities.....	65,200	30,242	76,835
Cash flows from investing activities:			
Net (purchases of) proceeds from the sale of short-term investments.....	(11,900)	4,401	(4,401)
Purchases of property and equipment.....	(13,738)	(48,836)	(21,110)
Proceeds from the disposition of property and equipment.....	14	1,445	6,640
Lease incentives granted.....	432	2,561	886
Acquisition of license.....	(741)	(2,975)	(5,000)
Purchases of long-term investments.....	842	(1,435)	(173)
Net cash used by investing activities.....	(25,091)	(44,839)	(23,158)
Cash flows from financing activities:			
Proceeds from notes payable and long-term debt.....	102,300	163,935	176,289
Repayment of notes payable and long-term debt.....	(144,817)	(149,734)	(174,308)
Proceeds from issuance of common stock.....	--	--	115,300
Repayments of S distribution notes.....	--	--	(129,000)
Distributions to stockholders.....	--	--	(39,600)
Net cash provided (used) by financing activities.....	(42,517)	14,201	(51,319)
Effect of exchange rates on cash.....	57	(200)	25
Net increase (decrease) in cash.....	(2,351)	(596)	2,383
Cash at beginning of year.....	8,204	8,800	6,417
Cash at end of year.....	\$ 5,853	\$ 8,204	\$ 8,800
Supplemental disclosures			
Cash paid during the year for:			
Interest.....	\$ 15,095	\$ 15,185	\$ 14,246
Income taxes.....	\$ 3,704	39,558	14,703

On January 2, 1997, in connection with acquisition of a license, the Company issued 216,216 shares of Common Stock aggregating \$3.0 million.

See accompanying notes to consolidated financial statements

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 1998 AND 1997

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND PRACTICES

Guess ?, Inc. ("the Company" or "Guess") designs, develops, and markets quality contemporary jeans and other casual wear for men, women and girls. The Company distributes its products through major department stores, specialty retailers, foreign distributors and its network of Company-owned and -operated retail and factory outlet stores. The company also licenses its trademarks under licensing arrangements for the sale of product in the United States and internationally.

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of Guess ?, Inc. and its wholly-owned foreign subsidiary, Guess Europe, B.V., a Netherlands corporation ("GEBV"). GEBV holds three wholly owned subsidiaries: Ranche, Limited, a Hong Kong corporation ("Ranche"), Guess Asia, a Hong Kong corporation, and Guess? Italia, S.r.l., an Italian corporation ("Guess? Italia"). Accordingly, all references herein to "Guess ?, Inc." include the consolidated results of the Company and its subsidiaries. All intercompany accounts and transactions are eliminated during the consolidation process.

INVESTMENT SECURITIES

The Company accounts for its investment securities in accordance with Financial Accounting Standards Board Statement No. 115, "Accounting for Certain Investments in Debt and Equity Securities" ("SFAS 115"). SFAS 115 requires investments to be classified into one of three categories based on management's intent: held-to-maturity securities, available-for-sale securities and trading securities. Held-to-maturity securities are recorded at amortized cost. Available-for-sale securities are recorded at fair value with unrealized gains and losses reported as a separate component of stockholders' equity. Trading securities are recorded at market value with unrealized gains and losses reported in operations. The Company accounts for its short-term investment securities as available-for-sale.

EARNINGS PER SHARE

Basic earnings per share represents net earnings divided by the weighted-average number of common shares outstanding for the period. Diluted earnings per share represents net earnings divided by the weighted-average number of shares outstanding, inclusive of the dilutive impact of common stock equivalents.

The reconciliation of basic to diluted weighted average shares is as follows (in thousands):

	1998	1997	1996 ----- (PRO FORMA)
Net earnings used for basic and diluted earnings per share.....	\$ 25,111	\$ 37,511	\$ 49,326
Weighted average shares used in basic computations.....	42,904	42,898	41,906
Dilutive stock options.....	15	4	2
Weighted average shares used in diluted computation.....	42,919	42,902	41,908

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND PRACTICES (CONTINUED)

Options to purchase 1,036,000, 1,421,000, and 1,162,000 shares of common stock at prices ranges from \$5.50 to \$11.00, \$10.50 to \$18.00 and \$18.00 were outstanding during 1998, 1997 and 1996, respectively, but were not included in the computation of diluted earnings per share because the options exercise prices were greater than the average market price of the common shares.

CONCENTRATION OF CREDIT RISK

The Company's financial instruments that are exposed to concentrations of credit risk consist primarily of cash equivalents and accounts receivable. The Company maintains cash and cash equivalents with various major financial institutions and performs evaluations of the relative credit standing of these financial institutions in order to limit the amount of credit exposure with any institution. The Company extends credit to corporate customers based upon an evaluation of the customer's financial condition and credit history and generally requires no collateral. The Company's customers are principally located throughout North America, and their ability to pay amounts due to the

Company may be dependent on the prevailing economic conditions of their geographic region. However, such credit risk is considered limited due to the Company's large customer base. Management performs regular evaluations concerning the ability of its customers to satisfy their obligations and records a provision for doubtful accounts based on these evaluations. The Company's credit losses for the periods presented are insignificant and have not exceeded management's estimates. No single customer accounted for a significant amount of consolidated net revenue for the years ended December 31, 1998, 1997 or 1996.

INVENTORIES

Inventories are stated at the lower of cost (first-in, first-out) or market.

REVENUE RECOGNITION

The Company recognizes wholesale revenue from the sale of merchandise upon shipment and for retail operations, at point of sale. Royalty income is based upon a percentage, as defined in the underlying agreement, of the licensees' net revenue. The Company accrues for estimated sales returns and allowances in the period in which the related revenue is recognized.

DEPRECIATION AND AMORTIZATION

Depreciation and amortization of property and equipment are provided using the straight-line method over the following useful lives:

Building and building improvements.....	18 to 31 years
Land improvements.....	5 years
Machinery and equipment.....	3 to 5 years
Corporate aircraft.....	7 years
Corporate vehicles.....	3 years
Shop fixtures.....	5 years

Leasehold improvements are amortized over the lesser of the estimated useful life of the asset or the term of the lease. Construction in progress is not depreciated until the related asset is completed.

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND PRACTICES (CONTINUED)

Goodwill, which represents the excess of purchase price over fair value of net assets acquired, is amortized on a straight-line basis over the expected periods to be benefited, generally 15 years.

FOREIGN CURRENCY TRANSLATION

In accordance with SFAS 52, "Foreign Currency Translation", balance sheet accounts of the Company's foreign operations are translated from foreign currencies into U.S. dollars at year-end or historical rates while income and expenses are translated at the weighted-average exchange rates for the year. The related translation adjustments are reflected as a foreign currency translation adjustment in the consolidated balance sheet.

INCOME TAXES

Prior to the IPO in August 1996, the Company had elected to be taxed as an S corporation for Federal income tax purposes. In certain states, the Company was

taxed as an S corporation, including California, in other states, the Company was taxed as a C corporation. As a result of the Company's IPO, all S corporation elections were terminated.

The Company uses the asset and liability method of accounting for income taxes. Under this method, deferred income taxes are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to be applied to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date.

COMPREHENSIVE INCOME

In June 1997, the FASB issued Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" ("SFAS 130"). The Company adopted SFAS 130 effective January 1, 1998. SFAS 130 establishes standards for the reporting and presentation of comprehensive income and its components in a full set of financial statements. Comprehensive income consists of net earnings and foreign currency translation adjustments and is presented in the consolidated statements of stockholders' equity and comprehensive income (loss). The Statement requires only additional disclosures in the consolidated financial statements; it does not affect the Company's financial position or results of operations. Prior year consolidated financial statements have been reclassified to conform to the requirements of SFAS 130.

BUSINESS SEGMENT REPORTING

The Company adopted SFAS 131 "Disclosures About Segments of an Enterprise and Related Information", effective in 1998. SFAS No. 131 establishes new standards for reporting information about business segments and related disclosures about products and services, geographic areas and major customers. The business segments of the Company are wholesale, retail and licensing operations. Information to these segments is summarized in note 12.

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND PRACTICES (CONTINUED) PRO FORMA NET EARNINGS

Pro forma net earnings represent the results of operations adjusted to reflect a provision for income taxes on historical earnings before income taxes, which gives effect to the change in the Company's income tax status to a C corporation as a result of the public sale of its Common Stock. Following the Company's IPO and the subsequent termination of its S corporation status on August 12, 1996, the Company recorded net deferred tax assets aggregating \$11.0 million, representing the difference between financial reporting and tax bases of assets and liabilities, using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The principal difference between the pro forma income tax rate and the Federal statutory rate of 35% relates primarily to state income taxes.

Actual and pro forma basic earnings per share have been computed by dividing net and pro forma earnings by the weighted-average number of actual shares of Common Stock outstanding during the period. Options to purchase Common Stock are included in the calculation of diluted earnings per share, provided their impact is not anti-dilutive.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amount of the Company's financial instruments, which principally include cash, short and long-term investments, trade receivables, accounts payable and accrued expenses, approximates fair value due to the relatively short maturity of such instruments.

The fair value of the Company's debt instruments are based on the amount of future cash flows associated with each instrument discounted using the Company's borrowing rate. At December 31, 1998 and 1997, the carrying value of all financial instruments was not materially different from fair value.

USE OF ESTIMATES

Management of the Company has made a number of estimates and assumptions relating to the reporting of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements in conformity with generally accepted accounting principles. Actual results could differ from these estimates.

LONG-LIVED ASSETS

It is the Company's policy to account for long-lived assets, including intangibles, at the lower of amortized cost or fair value, less disposition costs. Long-lived assets and certain identifiable intangibles are reviewed for impairment wherever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If this assessment indicates that the intangibles will not be recoverable, as determined by a non-discounted cash flow generated by the asset, the carrying value of the Company's long-lived assets would be reduced to its estimated fair market value based on the discounted cash flows.

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

ADVERTISING COSTS

The Company expenses the cost of advertising as incurred. Advertising expenses charged to operations for the years ended December 31, 1998, 1997 and 1996 were \$18.0 million, \$22.5 million and \$23.6 million, respectively.

RECLASSIFICATIONS

Certain reclassifications have been made to the 1996 and 1997 financial statements to conform to the 1998 presentation.

(2) INVESTMENTS

Short-term investments consist of overnight interest bearing deposit accounts aggregating \$11.9 million at December 31, 1998.

Long-term investments consist of certain debt and equity securities aggregating \$1.1 million and \$2.3 million at December 31, 1998 and 1997, respectively. The majority of these investments are primarily related to the Company's ownership interests in companies which are accounted for under the equity method. See also "note 8 - Related Party Transactions."

(3) INVENTORIES

Inventories are summarized as follows (in thousands):

1998

1997

Raw materials.....	\$ 9,400	\$ 13,437
Work in process.....	7,922	8,059
Finished goods--wholesale.....	35,465	38,599
Finished goods--retail.....	36,712	31,986
	-----	-----
	\$ 89,499	\$ 92,081
	-----	-----

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(4) PROPERTY AND EQUIPMENT

Property and equipment is summarized as follows (in thousands):

	1998	1997
	-----	-----
Land and land improvements.....	\$ 5,729	\$ 5,729
Building and building improvements.....	8,462	8,462
Leasehold improvements.....	59,218	59,174
Machinery and equipment.....	71,975	71,057
Corporate aircraft.....	5,973	5,725
Shop fixtures.....	28,895	24,665
Construction in progress.....	1,321	240
	-----	-----
	181,573	175,052
Less accumulated depreciation and amortization.....	95,120	76,882
	-----	-----
	\$ 86,453	\$ 98,170
	-----	-----

Construction in progress at December 31, 1998 and 1997 represents the costs associated with the construction of buildings and improvements used in the Company's operations and other capitalizable expenses in progress.

(5) NOTES PAYABLE AND LONG-TERM DEBT

Notes payable and long-term debt are summarized as follows (in thousands):

	1998	1997
	-----	-----
	(IN THOUSANDS)	
9 1/2% Senior Subordinated Notes due 2003.....	\$ 99,000	\$ 105,000
Advances under a secured \$100,000,000 long-term line of credit with a syndicate of banks; interest is variable, with an average annual effective rates of 7.27% in 1998 and 7.98% in 1997, respectively, and interest payable monthly.....	--	36,300
Note payable, secured by corporate aircraft, bearing interest at 8.23% per year, payable in quarterly principal and interest installments of \$221,003 through March 1998.....	--	217
	-----	-----
	99,000	141,517
Less current installments.....	--	217
	-----	-----
Long-term debt, excluding current installments.....	\$ 99,000	\$ 141,300
	-----	-----

The Credit Agreement contains various restrictive covenants requiring, among other things, the maintenance of certain financial ratios. The Company was in compliance with all such covenants as of December 31, 1998. Under the line of credit, the Company had \$1.7 million in outstanding standby letters of credit and \$11.3 million in outstanding commercial letters of credit as of December 31, 1998. In addition, the arrangements governing the Company's Credit Agreement and the indenture pursuant to which the Senior Subordinated Notes were issued restrict the payments of dividends by the Company.

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(5) NOTES PAYABLE AND LONG-TERM DEBT (CONTINUED)

The Senior Subordinated Notes are redeemable at the option of the Company, in whole or in part, on or after August 15, 1998, at various redemption prices. In December 1998 and February 1999, the Company repurchased \$6.0 million and \$4.0 million of its Senior Subordinated Notes, respectively.

(6) INCOME TAXES

Income taxes, including the pro forma income taxes giving effect as if the Company had been a C corporation throughout all of 1996, is summarized as follows (in thousands):

	YEAR ENDED DECEMBER 31,		
	1998	1997	1996
Federal:			
Current.....	\$ 14,477	\$ 17,487	\$ 33,686
Deferred.....	793	2,995	(7,449)
State:			
Current.....	2,459	3,973	7,339
Deferred.....	41	(1,212)	(693)
Foreign:			
Current.....	410	801	358
	<u>\$ 18,180</u>	<u>\$ 24,044</u>	<u>\$ 33,241</u>

The Company's statement of earnings for 1996 includes a provision for income taxes of \$15.8 million, which principally represents the Federal and state income taxes recorded from the date of the S corporation election termination, August 12, 1996, through December 31, 1996.

The actual pro forma income taxes differs from the expected income taxes obtained by applying the statutory Federal income tax rate to earnings before income taxes as follows (in thousands):

	YEAR ENDED DECEMBER 31,		
	1998	1997	1996
Computed "expected" tax expense.....	\$ 15,152	\$ 21,544	\$ 28,924
State taxes, net of Federal benefit.....	1,625	2,928	4,109
Foreign.....	(14)	(157)	--
U.S. tax and foreign withholding tax on foreign distributions.....	739	--	--

Other.....	678	(271)	208
	-----	-----	-----
	\$ 18,180	\$ 24,044	\$ 33,241
	-----	-----	-----

The income tax expense for the year ended December 31, 1997 includes taxes of \$2.7 million related to a one-time change in accounting (see also note 16). The Company's consolidated statement of earnings has presented the change in accounting net of this income tax expense.

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(6) INCOME TAXES (CONTINUED)

Deferred income tax reduction (benefit) from the following for the years ended December 31, 1998, 1997 and 1996 (in thousands):

	YEAR ENDED DECEMBER 31,		
	1998	1997	1996
	-----	-----	-----
Uniform capitalization.....	\$ 98	\$ (1,206)	\$ --
Deferred rent.....	(214)	(524)	--
Deferred lease incentives.....	476	(662)	--
Bad debt and other reserves.....	877	(2,352)	(981)
Depreciation and gain on sale of fixed assets.....	(2,125)	6,144	(4,101)
Write-down of investments.....	(312)	1,062	--
State taxes.....	521	(100)	(2,569)
Other.....	1,513	(579)	(491)
	-----	-----	-----
	\$ 834	\$ 1,783	\$ (8,142)
	-----	-----	-----

The tax effects of temporary differences that give rise to significant portions of current and non-current deferred tax assets and deferred tax liabilities at December 31, 1998 and 1997 are presented below (in thousands):

	1998	1997
	-----	-----
Deferred Tax Assets:		
Retail store closure reserves.....	\$ 467	\$ 1,130
Deferred lease incentives.....	1,648	2,124
Rent expense.....	2,158	1,944
Uniform capitalization adjustment.....	1,987	2,086
State income taxes.....	870	902
Bad debt and other reserves.....	1,810	2,688
Other.....	2,065	2,985
	-----	-----
Total gross deferred assets.....	11,005	13,859
Less: Valuation allowance.....	--	--
Less: Deferred tax liabilities.....	(400)	(2,420)
	-----	-----
Net deferred tax assets.....	\$ 10,605	\$ 11,439
	-----	-----

Included above at December 31, 1998 and 1997 are \$6.5 million and \$9.4 million for current deferred tax assets, respectively and \$4.1 million and \$2.0 million for non-current deferred tax assets, which are included in other assets.

GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

Based on the historical earnings of the Company, Management believes it is more likely than not that the results of operations will generate sufficient taxable earnings to realize net deferred tax assets.

(7) STOCKHOLDERS' EQUITY

On January 2, 1997, the Company issued 216,216 shares of Common Stock at \$13.87 per share in connection with an Asset Purchase Agreement, whereby the Company purchased the rights, title and interest to the then existing license agreement between the Company and Sweatshirt Apparel U.S.A., Inc. for the manufacturing and distribution rights for Guess women's knitwear products. The aggregate purchase price was \$10.0 million, of which \$5.0 million was paid in cash in the fourth quarter of 1996, \$2.0 million was paid in cash in the first quarter of 1997 and the balance of \$3.0 million was paid in the form of the aforementioned stock issuance.

In connection with the Company's IPO of 7,000,000 shares of Common Stock at \$18.00 per share, which took place on August 7, 1996, (i) Marciano International, which was owned by the Marciano Trusts and held an interest in the subsidiaries of Guess, was merged with and into the Company; (ii) all of the capital stock of Guess? Italia was contributed to GEBV; (iii) the Company effected a 32.66 to 1 split of the Common Stock; (iv) the Company declared a distribution of \$185.0 million to the Principal Stockholders, representing the Company's previously taxed and undistributed S corporation earnings which included a distribution of \$54.0 million (3,000,000 shares at \$18.00 per share) of Common Stock, \$129.0 million in cash generated primarily from the IPO and \$2.0 million in S Distribution Notes; (v) the Company terminated its status as an S corporation; and (vi) the Company granted options to purchase 1,225,673 shares pursuant to the Company's 1996 Equity Incentive Plan with an exercise price equal to the IPO price of \$18.00 per share.

(8) RELATED PARTY TRANSACTIONS

The Company is engaged in various transactions with entities affiliated with trusts for the respective benefit of Maurice, Paul and Armand Marciano (the "Marciano Trusts"). The Company believes that the arrangements involving each of the companies in which the Marciano Trusts have an investment, and related party transactions discussed below were entered into on terms no less favorable to the Company than could have been obtained from an unaffiliated third party.

LICENSE AGREEMENTS AND LICENSEE TRANSACTIONS

On September 28, 1990, the Company entered into a license agreement with Charles David of California ("Charles David"). Charles David is controlled by the father-in-law of Maurice Marciano. The Marciano Trusts and Nathalie Marciano (the spouse of Maurice Marciano) together own 50% of Charles David, and the remaining 50% are owned by the father-in-law of Maurice Marciano. The license agreement grants Charles David the rights to manufacture worldwide and distribute worldwide (except Japan and certain European countries) for men, women and some children, leather and rubber footwear, excluding athletic footwear, which bear the Guess trademark. The license also includes related shoe care products and accessories. Gross royalties earned by the Company under such license agreement for the fiscal years ended December 31, 1998, 1997 and 1996 were \$1.4 million, \$1.2 million and \$1.5 million, respectively. Additionally, the Company purchased \$6.1 million, \$6.1 million and \$6.0 million of products from Charles David for resale in the Company's retail stores during the same periods.

GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(8) RELATED PARTY TRANSACTIONS (CONTINUED)

On September 1, 1994, the Company entered into a license agreement with California Sunshine Activewear, Inc. ("California Sunshine"), granting it the rights to manufacture and distribute men's and women's activewear, which bear the Guess trademark, in the United States. Effective as of June 30, 1998, 51% of the shares of California Sunshine, formerly owned by the Marciano Trusts, were sold back to California Sunshine. Gross royalties earned by the Company under such license agreement for the fiscal years ended December 31, 1998, 1997 and 1996 were \$0.7 million, \$1.0 million and \$0.7 million, respectively. Additionally, the Company purchased \$0.4 million, \$1.5 million and \$1.4 million of products from California Sunshine for resale in the Company's retail stores during the same respective periods.

Effective January 1, 1995, the Company entered into a license agreement with Guess? Italia, S.r.l. ("Guess? Italia"), granting it exclusive rights in Italy and non-exclusive rights in certain other countries within Europe to manufacture and distribute men's and women's apparel and accessories which bear the Guess trademark. This license agreement was terminated in May 1997 in connection with the sale of the wholesale operations of Guess? Italia (see also "Maco Apparel, S.p.a." discussion below). The Company and Guess? Italia also entered into a retail store license agreement as of January 1, 1995, whereby Guess? Italia was granted the non-exclusive rights to operate Guess stores in Italy. Additionally, effective as of June 1, 1998, the Company entered into a license agreement with Guess? Italia, granting it exclusive rights within certain European countries to manufacture and distribute Guess Women's Collection apparel products which bear the Guess trademark. Prior to the IPO, Guess? Italia was owned 79% by the Company and 21% by Marciano International, a company wholly-owned by the Marciano Trusts. As part of the reorganization and in connection with the IPO, Guess? Italia became a wholly owned subsidiary of the Company when Marciano International was merged with and into the Company. Gross royalties earned by the Company under such license agreement for the fiscal years ended December 31, 1998, 1997 and 1996 were \$0.0 million, \$0.6 million and \$0.8 million, respectively. Additionally, the Company purchased \$0.0 million, \$0.2 million and \$0.3 million of product from Guess? Italia and sold \$0.1 million, \$0.0 million and \$0.1 million of product to Guess? Italia for resale in its retail store and to other wholesale customers during the fiscal years ended December 31, 1998, 1997 and 1996, respectively.

In May 1997, the Company sold substantially all of the assets and liabilities of Guess? Italia to Maco Apparel, S.p.a. ("Maco"). The effect of the net asset disposal was immaterial to the Company's results of operations. In connection with this sale, the Company also purchased a 10% ownership interest in Maco and entered into an approximate 10-year license agreement with Maco granting it the right to manufacture and distribute certain men's and women's jeanswear apparel, which bear the Guess trademark, in certain parts of Europe. In addition to royalty fees, the Company will also receive \$14.1 million over the a four year period in consideration of the grant of the license rights for men's and women's jeanswear apparel. During 1998 and 1997, the Company recorded \$2.8 million and \$2.6 million, respectively, in revenue in connection with the grant of such license rights. Additionally, the Company also recorded \$2.3 million and \$1.0 million in royalty fees related to product sales in 1998 and 1997, respectively. Effective as of March 1, 1998, the Company also entered into an approximate nine-year license agreement with Maco granting it the right to manufacture and distribute kid's jeanswear, which bear the Guess trademark, in certain parts of Europe.

Effective December 9, 1992, the Company entered into a license agreement with Nantucket Industries, Inc. ("Nantucket"), granting it the rights to manufacture and distribute within the United States women's intimate apparel which bear the Guess trademark. Nantucket is owned 13.1% by the Company

GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(8) RELATED PARTY TRANSACTIONS (CONTINUED)

and 3.8% by the trusts for the respective benefit of Paul Marciano and Armand Marciano. With respect to Nantucket, during the fiscal years ended December 31, 1998, 1997 and 1996, the Company recorded gross royalty income of \$0.1 million, \$0.8 million and \$0.3 million, respectively; purchased \$0.1 million, \$0.3 million and \$0.4 million, respectively, of product for resale in its retail stores; and recorded equity losses of \$0.0 million, \$0.2 million and \$0.3 million, respectively. In December 1997, Maurice Marciano sold all of the shares of Nantucket common stock held by his trust, which collectively gave the Company and its affiliates less than a 20% ownership in Nantucket. Accordingly, effective December 1997, the Company discontinued recording equity income or losses from this investment with respect to Nantucket. In connection with the lower aggregate percentage of ownership in Nantucket, in December 1997 the Company changed from the equity income method to the lower of cost or market method of valuing this investment, which resulted in an additional \$1.4 million loss in the fourth quarter of 1997 and \$0.3 million for 1998. Effective March 31, 1998, the license agreement between the Company and Nantucket was terminated. As a result of this termination, Nantucket agreed that it would cease all sales of its Guess products by April 30, 1998.

Effective December 1, 1989, the Company entered into a license agreement with Strandel, Inc. ("Strandel"), granting it the rights to manufacture and distribute in Canada men's, women's and children's knits and woven sportswear, which bear the Guess trademark. Strandel is owned 20% by the Company. With respect to Strandel, during the fiscal years ended December 31, 1998, 1997 and 1996, the Company recorded gross royalty income of \$1.6 million, \$1.6 million and \$1.8 million, respectively, and recorded equity losses of \$0.2 million, \$0.1 million and \$0.1 million, respectively.

On January 1, 1997, the Company acquired a 50% interest in Cignal, Limited, a Hong Kong corporation. With respect to Cignal, during the fiscal years ended December 31, 1998 and 1997, the Company recorded \$0.0 million and \$0.1 million of royalty income, respectively, and \$0.1 million and \$0.1 million of equity losses, respectively. Effective September 30, 1998, the license agreement between the Company and Cignal Limited, which granted Cignal the right to manufacture and distribute Guess men's and women's underwear, lingerie and sleepwear in New Zealand, Australia, Canada and parts of Southeast Asia, was terminated by mutual consent. As a result of this termination, Cignal agreed that it would cease all sales of its Guess products by December 31, 1998.

On January 1, 1997, the Company acquired from Pour le bebe, Inc., a California corporation, a 24.75% limited partnership interest in S.W.P.I., Ltd., a California limited partnership, as payment in lieu of unpaid license fees due November 1, 1996. The Marciano Trusts have a 75.25% ownership interest in S.W.P.I., Ltd. The 24.75% limited partnership in S.W.P.I., Ltd. was valued at \$1.4 million by the Company, based on the fair market value of the real estate limited partnership. During the fiscal years ended December 31, 1998 and 1997, the Company recorded \$0.2 million and \$0.0 million, respectively, of equity income associated with the real estate limited partnership. Additionally, in 1998, the Company received a cash dividend of \$0.8 million from S.W.P.I., Ltd.

BUYING AGENCY AGREEMENT

In February 1996, the Company entered into a buying agency agreement with Newtimes Guess?, Ltd. ("Newtimes"). The Company owns 50% of Newtimes. Pursuant to such agreement, the Company pays Newtimes a commission based on the cost of finished garments purchased for the Company. Commissions earned by Newtimes from the Company during the fiscal years ended December 31, 1998 and 1997 were

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(8) RELATED PARTY TRANSACTIONS (CONTINUED)

\$1.0 million and \$1.7 million, respectively. Additionally, with respect to Newtimes, the Company recorded \$0.0 million and \$0.1 million in equity losses during the fiscal year ended December 31, 1998 and 1997, respectively. During 1998, Newtimes was dissolved after the Company terminated its buying agency agreement with them, as well as severed its equity interest. Accordingly, the Company has discontinued recording equity income during 1998.

LEASES

The Company leases manufacturing, warehouse and administrative facilities from partnerships affiliated with the Marciano Trusts and certain of its affiliates (the "Principal Stockholders"). There are two leases in effect at December 31, 1998, both of which expire in July 2008. The total lease payments to these limited partnerships are currently \$220,000 per month. Additionally, the Company is also on a month to month lease for another storage facility. Aggregate lease payments under leases in effect for the fiscal years ended December 31, 1998, 1997 and 1996 were \$2.7 million, \$2.6 million and \$2.9 million, respectively.

Effective August 1, 1996, the Company subleased, on a month-to-month basis, a portion of a Guess facility to Southwest Pacific Investment Company ("SWPI"), an entity owned by the Marciano Trusts. During the fiscal years ended December 31, 1997 and 1996, rental income recorded with respect to SWPI aggregated \$0.1 million and \$0.1 million, respectively. The month-to-month sublease with SWPI was terminated on December 31, 1997.

(9) COMMITMENTS AND CONTINGENCIES

LEASES

The Company leases its showrooms and retail store locations under operating lease agreements expiring on various dates through May 2012. Some of these leases require the Company to make periodic payments for property taxes and common area operating expenses. Certain leases include rent abatements and scheduled rent escalations, for which the effects are being amortized and recorded over the lease term. The Company also leases some of its equipment under operating lease agreements expiring at various dates through May 2003.

Future minimum rental payments under non-cancelable operating leases at December 31, 1998 are as follows:

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(9) COMMITMENTS AND CONTINGENCIES (CONTINUED)

Year ending December 31, (in thousands):

	NON RELATED PARTIES	RELATED PARTIES	TOTAL
	-----	-----	-----
1999.....	\$ 24,903	\$ 2,639	\$ 27,542
2000.....	24,502	2,639	27,141
2001.....	23,981	2,639	26,620
2002.....	22,153	2,639	24,792

2003.....	20,456	2,639	23,095
Thereafter.....	51,359	12,096	63,455
	-----	-----	-----
	\$ 167,354	\$ 25,291	\$ 192,645
	-----	-----	-----

Rental expense for all operating leases during the years ended December 31, 1998, 1997, and 1996 aggregated \$32.6 million, \$30.8 million, and \$26.4 million, respectively.

INCENTIVE BONUSES

Certain officers and key employees of the Company are entitled to incentive bonuses, primarily based on the Company's profits.

LITIGATION

On August 7, 1996, a class action complaint naming the Company and certain of its independent contractors was filed in the Superior Court of the State of California for the County of Los Angeles, titled as Brenda Figueroa et. al. v. Guess ?, Inc. et. al. (Case No. BC 155 165). In this case, an alleged class action, plaintiffs assert claims for violation of state wage and hour laws, wrongful discharge, and breach of contract arising out of the Company's relationship with its independent contractors and actions taken by the Company's independent contractors with respect to the employees of such independent contractors. Plaintiffs also allege that the Company breached its agreement with the United States Department of Labor regarding the monitoring of its independent contractors. The Court has held two hearings on certifying the alleged class. While the Court has not announced a final ruling, the Court has indicated it likely will at least certify a class of plaintiffs who allege wrongful termination claims.

The Union of Needletrades, Industrial and Textile Employees ("UNITE") has filed with the National Labor Relations Board ("NLRB") various charges that the Company is engaging in unfair labor practices within the meaning of the National Labor Relations Act ("NLRA"). These charges include allegations that the Company has unlawfully threatened to move its production outside the United States. These allegations have been dismissed by the Regional Director for Region 21 of the NLRB, and the NLRB has rejected UNITE's appeal of the dismissal.

On July 7, 1998, UNITE filed charges against the Company alleging that the Company violated the NLRA by failing to uphold certain obligations under a prior settlement agreement with the NLRB, by denying pro-union employees access to the Company's facilities, by conferring new benefits to employees, by making false accusations against UNITE, by conducting video surveillance of UNITE's offices, and by

GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(9) COMMITMENTS AND CONTINGENCIES (CONTINUED)

assisting and organizing an anti-union demonstration. The NLRB has not issued a ruling on these charges. These allegations have been dismissed by the Regional Director for Region 21 of the NLRB.

On February 24, 1998, the Company and Maurice Marciano, Paul Marciano and Armand Marciano, as individuals, were named as defendants in a class action entitled John N. Robinson v. Guess ?, Inc., Maurice Marciano, Paul Marciano and Armand Marciano, Case No. BC186583, filed in the Los Angeles Superior Court. The complaint (the "Complaint") purported to state a claim under Sections 11, 12(a)(2) and 15 of the Securities Act of 1933 for alleged misrepresentations in connection with the Company's initial public offering (the "IPO") in August

1996. Mr. Robinson purported to represent a class of all purchasers of the Company's stock in the IPO and sought unspecified damages.

On October 1, 1998, Mr. Robinson filed an amended complaint ("The Amended Complaint") naming the same parties as defendants. In the Amended Complaint, Mr. Robinson purports to represent the same class of purchasers of the Company's stock in its IPO. As in the original complaint, the Amended Complaint purports to state claims under Sections 11, 12(a)(2) and 15 of the Securities Act of 1933 for alleged misrepresentations in connection with the Company's IPO. On December 15, 1998, the Company filed a Demurrer and Motion to Strike the Amended Complaint. While it is too soon to predict the outcome of the case with any certainty, the Company believes that it has meritorious defenses to each of the claims asserted and intends to vigorously defend itself.

On October 26, 1998, Maurice Marciano, Paul Marciano and Armand Marciano, as individuals, (the "Marcianos"), as well as the Company, were named as defendants in a shareholder's derivative complaint entitled John N. Robinson v. Maurice Marciano, Paul Marciano and Armand Marciano and Guess?, filed in the Los Angeles Superior Court. The complaint (the "Derivative Complaint") purports to state a claim for intentional breach of fiduciary duty, negligent breach of fiduciary duty, constructive fraud and abuse of control in connection with the Marcianos' management of the Company since its IPO. On January 11, 1999, the Marcianos filed a Demurrer and Motion to Strike the Derivative Complaint. The Company joined in the Demurrer and the Motion to Strike, both of which are set for hearing on March 25, 1999. While it is too soon to predict the outcome of the case with any certainty, the defendants believe they have meritorious defenses to each of the claims asserted and intend to vigorously defend themselves.

The Company believes the outcome of one or more of the above cases could have a material adverse effect on the Company's financial condition and results of operations.

(10) SAVINGS PLAN

On January 1, 1992, the Company established the Guess ? Inc. Savings Plan (the "Savings Plan") under Section 401(k) of the Internal Revenue Code. Under the Savings Plan, employees ("associates") may contribute up to 15% of their compensation per year subject to the elective limits as defined by IRS guidelines and the Company may make matching contributions in amounts not to exceed 1.5% of the associates' annual compensation. The Company's contributions to the Savings Plan for each of the three years ended December 31, 1998, 1997 and 1996 aggregated \$0.3 million.

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(11) QUARTERLY INFORMATION (UNAUDITED)

The following is a summary of the unaudited quarterly financial information for the years ended December 31, 1998 and 1997 (in thousands, except per share data):

YEAR ENDED DECEMBER 31, 1998	FIRST QUARTER	SECOND QUARTER	THIRD QUARTER	FOURTH QUARTER
Net revenue.....	\$ 110,768	\$ 98,068	\$ 130,138	\$ 132,957
Gross profit.....	46,452	44,235	54,782	54,383
Net earnings.....	7,951	3,440	9,639	4,081
Basic and diluted earnings per share.....	\$ 0.19	\$ 0.08	\$ 0.22	\$ 0.10

YEAR ENDED DECEMBER 31, 1998	FIRST QUARTER	SECOND QUARTER	THIRD QUARTER	FOURTH QUARTER
Net revenue.....	\$ 135,736	\$ 118,515	\$ 142,442	\$ 118,679
Gross profit.....	61,584	54,449	64,374	46,557
Earnings (loss) before income taxes and cumulative effect of change in accounting principle.....	23,746	13,519	21,699	(4,077)
Earnings (loss) before cumulative effect of change in accounting principle.....	14,052	8,528	13,106	(2,136)
Net earnings (loss).....	18,013	8,528	13,106	(2,136)
Basic and diluted earnings per share.....	\$ 0.42	\$ 0.20	\$ 0.31	\$ (0.05)

During the fourth quarter of 1997, the Company recorded approximately \$3 million in non-recurring general and administrative expenses and approximately \$10 million in markdowns and returns in excess of anticipated levels.

(12) SEGMENT INFORMATION

In accordance with the requirements of SFAS 131, "Disclosures about Segments of and Enterprise and Related Information," the Company's reportable business segments and respective accounting policies, policies of the segments are the same as those described in note 1. Management evaluates segment performance based primarily on revenue and earnings from operations. Interest income and expense is evaluated on a consolidated basis and not allocated to the Company's business segments.

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

Segment information is summarized as follows for the years ended December 31, 1998, 1997 and 1996 (in thousands).

	YEAR ENDED DECEMBER 31,		
	1998	1997	1996
Net revenue:			
Wholesale operations.....	\$ 212,504	\$ 250,040	\$ 288,046
Retail operations.....	222,624	215,873	209,828
Licensing operations.....	36,803	49,459	53,288
	\$ 471,931	\$ 515,372	\$ 551,162
Earnings from operations:			
Wholesale operations.....	\$ 8,209	\$ 16,179	\$ 33,143
Retail operations.....	12,034	5,008	11,664
Licensing operations.....	36,803	49,459	53,288
	\$ 57,046	\$ 70,646	\$ 98,095
Capital expenditures:			
Wholesale operations.....	\$ 8,136	\$ 19,225	
Retail operations.....	5,602	29,611	
Licensing operations.....	--	--	
	\$ 13,738	\$ 48,836	
Total assets			
Wholesale operations.....	\$ 159,069	\$ 175,361	
Retail operations.....	93,140	97,790	

Licensing operations.....	11,563	14,663
	-----	-----
	\$ 263,772	\$ 287,814
	-----	-----

The table below presents information related to geographic areas in which the Company operated in during 1998 and 1997 (in thousands).

	YEAR ENDED DECEMBER 31,		
	1998	1997	1996
Net sales:			
United States.....	\$ 434,207	\$ 455,969	\$ 484,359
Asia.....	13,859	22,277	19,149
Europe.....	10,600	19,812	31,261
South America.....	5,066	7,965	5,167
North America (non U.S.).....	4,050	4,423	4,407
Other.....	4,149	4,926	6,819
	-----	-----	-----
	\$ 471,931	\$ 515,372	\$ 551,162
	-----	-----	-----

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(13) STOCK OPTION PLAN

On July 30, 1996, the Board of Directors adopted the Guess ?, Inc. 1996 Non-Employee Directors' Stock Option Plan pursuant to which the Board of Directors may grant stock options to non-employee directors. This plan authorizes grants of options to purchase up to 500,000 shares of authorized but unissued Common Stock. At December 31, 1998, 1997 and 1996, there were 70,451, 28,886 and 0 options issued under this plan, respectively. Stock options are granted with an exercise price equal to the stock's fair market value at the date of grant. Stock options have ten-year terms and vest and become fully exercisable in increments of one-fourth of the shares granted on each anniversary from the date of grant.

On July 30, 1996, the Board of Directors adopted the Guess ?, Inc. 1996 Equity Incentive Plan (the "Plan") pursuant to which the Board of Directors may grant stock options to officers, key associates and consultants. The Plan authorizes grants of options to purchase up to 4,500,000 shares of authorized but unissued Common Stock. Stock options are granted with an exercise price equal to the stock's fair market value at the date of grant. Stock options have ten-year terms (five years in the case of an incentive stock option granted to a ten-percent shareholder) and vest and become fully exercisable after varying time periods from the date of grant based on length of service or specified performance goals.

At December 31, 1998, 1997 and 1996, there were 2,841,825, 3,208,645 and 3,248,895 additional shares available for grant under the Plan, respectively. The per share weighted-average fair value of stock options granted during 1998, 1997 and 1996 was \$4.24, \$9.75 and \$15.83, respectively on the dates of grant using the Black Scholes option-pricing model with the following weighted-average assumptions: 1998, 1997 and 1996 expected dividend yields of 0.0%, 0.0% and 0.0%, respectively, 1998, 1997 and 1996 risk-free interest rates of 4.87%, 6.50% and 6.57%, respectively, 1998, 1997 and 1996 volatility factors of 63%, 30% and 27%, respectively, and 1998, 1997 and 1996 expected lives of four years.

The Company applies APB Opinion No. 25 in accounting for its Plan and, accordingly, no compensation cost has been recognized for its stock options in the accompanying consolidated financial statements. Had the Company determined compensation based on the fair value at the grant date for its stock options under FASB Statement No. 123 ("SFAS No. 123"), the Company's pro forma net earnings and net earnings per share for the years ended December 31, 1998, 1997 and 1996 would have been reduced to the pro forma amounts indicated below (in thousands, except per share data):

	1998	1997	1996
	-----	-----	-----
Pro forma net earnings.....	\$ 24,574	\$ 35,222	\$ 48,287
Pro forma earnings per share.....	\$ 0.57	\$ 0.82	\$ 1.15

Pro forma net earnings reflect only options granted since the inception of the Plan on July 30, 1996. The full impact of calculating compensation cost for stock options under SFAS No. 123 is not reflected in the pro forma net earnings amounts presented above because compensation cost is reflected over the options' vesting period of four years.

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(13) STOCK OPTION PLAN (CONTINUED)

Stock option activity during the period indicated is as follows:

	NUMBER OF SHARES	WEIGHTED-AVERAGE EXERCISE PRICE
	-----	-----
Balance at July 30, 1996.....	--	\$ --
Granted.....	1,287,105	17.74
Exercised.....	--	--
Forfeited.....	(36,000)	(18.00)
Expired.....	--	--
Balance at December 31, 1996.....	1,251,105	17.73
Granted.....	1,406,105	10.78
Exercised.....	--	--
Forfeited.....	(1,365,855)	(16.88)
Expired.....	--	--
Balance at December 31, 1997.....	1,291,355	\$ 11.05
Granted.....	1,035,600	4.24
Exercised.....	--	--
Forfeited.....	(668,780)	(10.92)
Expired.....	--	--
Balance at December 31, 1998.....	1,658,175	\$ 6.86

At December 31, 1998, 1997 and 1996, the weighted-average exercise price was \$6.86, \$11.05 and \$17.73, respectively, and the weighted-average remaining contractual lives of outstanding options were 9.0, 8.85 and 9.63 years, respectively.

The following table summarizes information about stock options outstanding and exercisable at December 31, 1998.

RANGE OF EXERCISE PRICES	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE	
	NUMBER OUTSTANDING AT DECEMBER 31, 1998	WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED AVERAGE EXERCISE PRICE	NUMBER EXERCISABLE AT DECEMBER 31, 1998	WEIGHTED AVERAGE EXERCISE PRICE
\$ 3.94 to \$ 5.58	981,100	9.8 years	\$ 4.18	0	\$ 0.00
9.00 to 11.00	677,075	7.9 years	10.73	315,875	10.84
	1,658,175	9.0 years	6.86	315,875	10.84

At December 31, 1997 and 1996, the number of options exercisable was 179,527 and 35,568, respectively. The weighted-average exercise price of those options was \$11.03 and \$18.00, respectively.

On August 11, 1997, the options granted on August 13, 1996, with an original exercise price of \$18.00, were repriced to \$11.00. All other terms of these options granted remained the same.

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(14) ACQUISITIONS

On December 4, 1996, the Company entered into an Asset Purchase Agreement in which the Company purchased the rights, title and interest to the existing License Agreement between the Company and Sweatshirt Apparel U.S.A., Inc. ("Sweatshirt Apparel"), for the manufacturing and distribution rights for Guess women's knitwear products. In connection with the Asset Purchase Agreement, the existing License Agreement between the Company and Sweatshirt Apparel was terminated on December 31, 1996. The aggregate purchase price was \$10.0 million, of which \$5.0 million was paid in cash prior to December 31, 1996, and \$2.0 million was paid in cash and \$3.0 million was settled in the form of a stock issuance, both of which occurred on January 2, 1997 (216,216 shares at \$13.87 per share). In addition, one of the Principal Stockholders of Sweatshirt Apparel will receive an earnout of no less than \$0.5 million for each of five years, commencing in 1997.

In May 1997, the Company formed a joint venture in Europe with the Fingen Group, a leading European apparel manufacturer and distributor owned by the Fratini family. The new joint venture, Maco Apparel, S.p.a., entered into a license agreement with the Company for the manufacture and sale of Guess jeanswear throughout Europe and purchased the Company's then-existing wholesale operations in Italy. Maco Apparel, S.p.a. produces a full collection of casual lifestyle jeanswear apparel, including men's and women's jeans. The Company will continue to design the collections to be sold in the European market. In addition, an affiliate of Maco Apparel, S.p.a., Fingen Apparel N.V., has entered into a retail store license agreement with the Company for the opening and operation of Guess retail stores throughout Europe.

(15) REORGANIZATION CHARGE

In the second quarter of 1996, the Company recorded a provision amounting to \$3.6 million for certain non-recurring charges relating to the write-down to net realizable value of operating assets associated with the (i) disposal of two currently active remote warehouse and production facilities, resulting in a net book loss of \$2.4 million, and (ii) the net book loss of \$1.2 million incurred

by the Company in connection with the sale of one of its aircraft.

The write-down to net realizable value related to the disposal of the warehouse and production facilities of \$2.4 million is based upon the asset carrying value of \$5.7 million less its appraisal value of \$3.9 million and includes a provision of \$.6 million for estimated disposal costs, comprised primarily of commissions, title fees and other customary real estate closing costs. The write-down related to the sale of the aircraft of \$1.2 million is based upon the asset carrying value of \$7.2 million less the sale price of \$6.0 million. The estimated costs of disposal of the aircraft were immaterial.

(16) CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING FOR PRODUCT DISPLAY FIXTURES

Effective January 1, 1997, the Company changed its method of accounting for product display fixtures located in its wholesale customers' retail stores, whereby the costs for such fixtures are capitalized and amortized over five years using the straight-line method. In prior years, these costs had been expensed as incurred. The Company believes that this new method will more closely match the long-term benefit that the product display fixtures provide with the expected future revenue from such fixtures. The cumulative effect of the change in accounting principle, recorded in the first quarter of 1997, is calculated based upon the retroactive effect of applying the new accounting method to prior year fixture acquisitions. The cumulative effect of the change in accounting principle of \$4.0 million (after reduction for income tax expense of \$2.7 million) is included in earnings for the year ended December 31, 1997. Excluding the

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GUESS ?, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 1998 AND 1997

(16) CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING FOR PRODUCT DISPLAY FIXTURES
(CONTINUED)

cumulative effect of the change in accounting principle, the effect of the change during 1997 was to increase net earnings by approximately \$6.2 million or \$0.14 per share.

(17) DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

The estimated value of financial instruments has been determined by the Company using available market information and valuation methodologies. Considerable judgement is required in estimated fair values. Accordingly, the estimates may not be indicative of the amounts the Company could realize in a current market.

The following methods were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate the value.

CASH AND CASH EQUIVALENTS

The carrying amount approximates fair value because of the short maturity of these instruments.

INVESTMENT SECURITIES

The fair value of the Company's investment securities is based on quoted market prices.

LONG-TERM DEBT

The fair value of the Company's long-term debt is estimated based on the current rates for similar issues or on the current rates offered to the Company for debt of similar remaining maturities.

NOTES RECEIVABLE/PAYABLE AND ADVANCES DUE TO/FROM RELATED PARTIES

It is not practicable to estimate the fair value of notes receivable or advances due to related parties and notes payable and advances due from related parties due to the nature of these instruments.

The estimated fair values of the Company's financial instruments are as follows (in thousands):

	DECEMBER 31, 1998		DECEMBER 31, 1997	
	CARRYING AMOUNT	FAIR VALUE	CARRYING AMOUNT	FAIR VALUE
Cash and cash equivalents.....	\$ 17,753	\$ 17,753	\$ 8,204	\$ 8,204
Investment securities.....	1,118	1,118	2,340	2,340
Long-term debt.....	99,000	97,515	105,000	107,888
Notes receivable/payable and advances Due to/from related parties.....	1,597	1,597	2,060	2,060

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SCHEDULE II

GUESS ?, INC. & SUBSIDIARIES

VALUATION AND QUALIFYING ACCOUNTS

YEARS ENDED DECEMBER 31, 1998, 1997, AND 1996

(IN THOUSANDS)

DESCRIPTION	BALANCE AT BEGINNING OF PERIOD	CHARGED TO COSTS AND EXPENSES	DEDUCTIONS AND WRITE-OFFS	BALANCE AT END OF PERIOD
As of December 31, 1996				
Allowance for obsolescence.....	\$ 4,360	\$ (218)	\$ (885)	\$ 3,257
Accounts receivable.....	10,849	4,263	(5,392)	9,720
As of December 31, 1997				
Allowance for obsolescence.....	3,257	3,764	(3,456)	3,565
Accounts receivable.....	9,720	12,746	(11,270)	11,196
As of December 31, 1998				
Allowance for obsolescence.....	3,565	3,512	(3,217)	3,860
Accounts receivable.....	11,196	8,542	(11,901)	7,837

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Los Angeles, State of California, on March 23, 1999.

GUESS ?, INC.

By: /s/ MAURICE MARCIANO

 Maurice Marciano
 CHAIRMAN OF THE BOARD,
 CHIEF EXECUTIVE OFFICER AND DIRECTOR

Pursuant to the requirements of the Securities Act of 1934, this report has been signed by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

NAME	TITLE	DATE
/s/ MAURICE MARCIANO ----- Maurice Marciano	Chairman of the Board, Chief Executive Officer and Director (Principal Executive Officer)	March 23, 1999
/s/ PAUL MARCIANO ----- Paul Marciano	President, Chief Operating Officer and Director	March 23, 1999
/s/ ARMAND MARCIANO ----- Armand Marciano	Senior Executive Vice President, Assistant Secretary and Director	March 23, 1999
/s/ BRIAN FLEMING ----- Brian Fleming	Executive Vice President and Chief Financial Officer (Principal Financial Officer and Chief Accounting Officer)	March 23, 1999
/s/ ALDO PAPONE ----- Aldo Papone	Director	March 23, 1999
/s/ ROBERT DAVIS ----- Robert Davis	Director	March 23, 1999
/s/ ALICE KANE ----- Alice Kane	Director	March 23, 1999

EXHIBIT INDEX

EXHIBIT NUMBER	DESCRIPTION
3.1	Restated Certificate of Incorporation of the Registrant. (1)
3.2	Bylaws of the Registrant. (1)
4.3	Specimen stock certificate. (1)
10.1	Amended and Restated Stockholders' Agreement. (2)
10.20	Amended and Restated Revolving Credit Agreement, dated as of March 28, 1997. (2)
10.22	1996 Equity Incentive Plan. (1)
10.23	1996 Non-Employee Directors' Stock Option Plan. (1)
10.24	Annual Incentive Plan. (1)
10.25	Employment Agreement between the Registrant and Maurice Marciano. (2)
10.26	Employment Agreement between the Registrant and Paul Marciano. (2)
10.27	Employment Agreement between the Registrant and Armand Marciano. (2)
10.28	Registration Rights Agreement among the Registrant and certain stockholders of the Registrant. (2)
10.29	Indemnification Agreement among the Registrant and certain stockholders of the Registrant. (2)
10.30	Indemnification Agreements between the Registrant and certain executives and directors. (2)
10.31	First Amendment to Amended and Restated Shareholders' Agreement. (3)
10.32	First Amendment and Waiver to Amended and Restated Revolving Credit Agreement by and between the Registrant and BankBoston, NA, F/K/A The First National Bank of Boston, Sanwa Bank California and the Financial Institutions Party hereto. (4)
10.33	Amended and Restated 1996 Non-Employee Directors' Stock Option Plan, as amended through March 3, 1997. (5)
10.34	Second Amendment and Consent to the Amended and Restated Revolving Credit Agreement by and between Guess ?, Inc. And BankBoston, N.A., F/K/A The First National Bank of Boston, Sanwa Bank California and the Financial Institutions Party Hereto. (6)
10.35	Third Amendment and Consent to the Amended and Restated Revolving Credit Agreement by and between Guess ?, Inc. And BankBoston, N.A., F/K/A The First National Bank of Boston, Sanwa Bank California and the Financial Institutions Party Hereto. (6)
10.36	Amendment No. 1 to The Guess ?, Inc. Amended and Restated 1996 Non- Employee Directors' Stock Option

Plan. (7)
10.37 Employment Agreement dated July 6, 1998 between Guess ?, Inc. and Brian L. Fleming. (7)
10.38 Fourth Amendment and Consent to the Amended and Restated Revolving Credit Agreement by and between Guess
?, Inc. And BankBoston, N.A., F/K/A The First National Bank of Boston, Sanwa Bank California and the
Financial Institutions Party Hereto. (8)
18.0 Letter regarding change in accounting principles. (5)
*21.1 List of Subsidiaries.
*27.1 Financial Data Schedule.

- - - - -
* Filed herewith

(b) Financial Statement Schedule:

Schedule II--Description Valuation and Qualifying Accounts
- - - - -

- (1) Incorporated by reference from the Registration Statement on Form S-1 (Registration No. 333-4419) filed by the Company on June 24, 1996, as amended.
- (2) Incorporated by reference from the Company's Annual Report on Form 10-K for the year ended December 31, 1996.
- (3) Incorporated by reference from the Company's Quarterly Report on Form 10-Q for the quarter ended March 30, 1997.
- (4) Incorporated by reference from the Company's Quarterly Report on Form 10-Q for the quarter ended June 29, 1997.
- (5) Incorporated by reference from the Company's Annual Report on Form 10-K for the year ended December 31, 1997.
- (6) Incorporated by reference from the Company's Quarterly Report on Form 10-Q for the quarter ended March 29, 1998.
- (7) Incorporated by reference from the Company's Quarterly Report on Form 10-Q for the quarter ended June 28, 1998.
- (8) Incorporated by reference from the Company's Quarterly Report on Form 10-Q for the quarter ended September 27, 1998.

EXHIBIT 23.1

LIST OF SUBSIDIARIES

Caption]

INVESTMENT IN	LOCATION	OWNED BY	PERCENT OF OWENERSHIP
Guess? Retail, Inc.	United States	Guess ?, Inc.	100%
Guess? Licensing, Inc.	United States	Guess ?, Inc.	100%
Guess? Europe, BV	Netherlands	Guess ?, Inc.	100%
Guess? Asia	Hong Kong	Guess? Europe, BV	100%
Ranche Ltd.	Hong Kong	Guess? Europe, BV	100%

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