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Dick's Sporting Goods, Inc. (DKS)

Q2 2015 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning and welcome to the DICK'S Sporting Goods Second Quarter 2015 Earnings Conference Call. All participants will be in listen-only mode. [Operation Instructions] After today's presentation, there will be an opportunity to ask questions. [Operation Instructions] Please note this event is being recorded.

I would now like to turn the conference over to Anne-Marie Megela, Vice President of Treasury Services and Investor Relations. Please go ahead.

Anne-Marie Megela

VP-Treasury Services & Investor Relations

Thank you.

Good morning and thank you for joining us to discuss our second quarter 2015 financial results. Please note that a rebroadcast of today's call will be archived on the Investor Relations portion of our website, located at DICKS.com for approximately 30 days. In addition, as outlined in our press release, the dial-in replay will also be available for approximately 30 days.

In order for us to take advantage of the Safe Harbor rules, I would like to remind you that today's discussion includes some forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, which includes, but are not limited to, our views and expectations concerning our future results. Such statements relate to future events and expectations and involve known and unknown risk and uncertainties. Our actual results or actions may differ materially from those projected in the forward-looking statements.

For a summary of the risk factors that could cause results to differ materially from those expressed in the forward-looking statement, please refer to our periodic reports filed with the SEC, including the company's Annual Report on Form 10-K for the year ended January 31, 2015. We disclaim any obligation and do not intend to update these statements except as required by the securities laws.

We've also included some non-GAAP financial measures in our discussion today. Our presentation of the most directly comparable financial measures, calculated in accordance with generally accepted accounting principles and related reconciliations can be found on the Investor Relations portion of our website at DICKS.com.

Leading our call today will be Ed Stack, our Chairman and Chief Executive Officer. Ed will review our second quarter results, key business drivers, and outlook. After Ed's comments, André Hawaux will provide greater detail regarding our results and guidance for the third quarter and full year 2015.

I will now turn the call over to Ed Stack.

Edward W. Stack

Chairman & Chief Executive Officer

Thank you, Anne-Marie. As we announced this morning, we generated second quarter earnings per diluted share of \$0.77, a 15% increase over last year, and above the high end of our guidance of \$0.73 to \$0.76. We drove this profitable growth primarily through new stores, an increase in consolidated same-store sales, continued momentum in eCommerce, and a meaningful margin rate expansion.

Second quarter consolidated same-store sales of 1.2% was within our guided range of flat to 2%, was on top of a 3.2% comp in the second quarter of 2014, which included substantial World Cup sales. DICK'S omni-channel comp sales increased 1.5% in the quarter, with growth across all of our three primary categories, hardlines, apparel and footwear.

Our focus on eCommerce continues to payoff, with eCommerce penetration growing to 7.3% of sales in the second quarter of this year, compared to 6.3% in the second quarter of 2014, reflecting growth of 24.4%.

Our golf business is beginning to show some encouraging trends. Our margins have improved significantly over last year, and the apparel side of our business has comped positively throughout the second quarter. Additionally, looking back at our golf business from the beginning of the year, we have experienced sequential improvement in our comp sales.

We have increased our inventory levels to begin the third quarter, supporting the accelerated sale in our outdoor category and to better capture the back-to-school business this year. At the end of Q3, we anticipate sales and inventory growth to more closely approximate each other.

Now let me provide a few updates on our growth drivers. We remain focused on driving store productivity through meaningful marketing and merchandising strategies. On the marketing front, we evolved our brand campaign this year asking a simple question, who will you be? We find the authenticity is really resonating with our customers. We have also formed a new partnership with Team USA and are now the official sporting goods retailer of the United States Olympic Committee. Through this partnership, we will provide equipment and jobs with flexible hours to our Olympic hopefuls. Additionally through our DICK'S Sporting Goods Foundation, we are expanding our Sports Matter program and deepening our commitment to youth athletics.

On the merchandising front, we remain particularly excited about our women's business, including our exclusive private brand offering CALIA by Carrie Underwood. This brand has performed better than expected and we continue to believe it will become our number three women's athletic apparel brand by the end of 2016.

Turning to eCommerce, we are progressing toward our goal of moving our DICK'S Sporting Goods eCommerce site onto our own platform by January 2017. As you will recall, last quarter we completed a key step by successfully relaunching GolfGalaxy.com, including ship-from-store capabilities and we remain on track to launch a Field & Stream transactional site later this year. The new Field & Stream site will not only allow us to capture incremental sales, but it will be able to operate and learn from having two sites on a single platform, which significantly leverages our costs.

Finally, we remain excited to grow our outdoor business. During the quarter, we opened our first combo store in Mobile, Alabama, featuring a DICK'S Sporting Goods and Field & Stream store under the same roof. We believe this new combined store concept will generate higher sales and store productivity as compared to our traditional stand-alone stores. The hunt, fish and camp product will all be in Field & Stream, leaving more room in the DICK'S stores for higher margin, faster turning categories. From a customer standpoint, they benefit from an expanded assortment and the ability to move between the stores once inside. We plan to have four of these combo stores in place by the end of 2015.

Taking into consideration our year-to-date results and our expectations for the balance of the year, we're raising our full year earnings guidance and now expect to deliver earnings per diluted share in the range of \$3.13 to \$3.21 and maintaining our 2015 full year consolidated comp growth range of 1% to 3%.

Of course, we would not be able to execute our growth plan without the hard work and commitment of our associates. I would like to thank all of them for their dedication and contribution to our progress.

Before concluding, I'd like to take a moment to welcome Teri List-Stoll to DICK'S Sporting Goods as Executive Vice President and Chief Financial Officer. Teri joins the company after an impressive 30-year career in finance. She served as EVP and Chief Financial Officer for Kraft Foods. Prior to joining Kraft, Teri was Senior Vice President and Treasurer at P&G, where she led the Global Treasury, Acquisition & Divestiture, Investor Relations and External Business Development organizations. We are very happy to have Teri on our team.

Andr  Hawaux, who most recently served in a temporary dual role as Executive Vice President, Chief Operating Officer and Chief Financial Officer, will now continue as our Executive Vice President, Chief Operating Officer. Andr  has done a great job as our CFO and I know he will continue to contribute meaningfully in his new role.

I'd now like to turn the call over to Andr .

Andr  J. Hawaux

Chief Operating Officer & Executive Vice President

Thank you, Ed, and thanks for the kind words. This morning, I will cover three topics: our second quarter results, our balance sheet, and our performance expectations for the remainder of 2015. To begin with our second quarter financial results, total sales increased 7.9% to approximately \$1.8 billion. Consolidated same-store sales increased 1.2% compared to our guidance of flat to 2%, and compared to comps of 3.2% in the second quarter of last year.

DICK'S Sporting Goods omni-channel same-store sales increased 1.5%, driven by a 2.5% increase in sales per transaction and a 1% decrease in traffic. This decrease in traffic is primarily attributable to the anniversary of last year's World Cup event and golf promotions.

In the second quarter of 2015, we continue to grow our omni-channel platform. We opened seven new DICK'S stores and generated 96.5% new store productivity. We opened one new Field & Stream store and closed three Golf Galaxy stores as these leases expired and these stores were not meeting our internal hurdle rates. Additionally, we grew our eCommerce business to 7.3% of sales compared to 6.3% in the second quarter of 2014.

Gross profit for the second quarter was \$554 million or 30.37% of sales, and was up 47 basis points year-over-year on a non-GAAP basis. This improvement in gross profit margin was primarily driven by less promotional activity as compared to the second quarter of last year and partially offset by occupancy deleverage.

SG&A expenses in the second quarter were \$396 million, or 21.72% of sales, and on a non-GAAP basis, de-leveraged 10 basis points from the second quarter of last year. This was primarily due to expenses related to the building out our brand, which were described by Ed earlier and planned investments in eCommerce.

Now, looking to our balance sheet, we ended the second quarter of 2015 with approximately \$123 million of cash and cash equivalents and no borrowings under our outstanding our revolving credit facility. Also, as disclosed this morning, we've amended and extended our revolving credit facility prior to its expiration in December of 2016, thereby benefiting from the attractive interest rate environment. We have increased our limit from \$500 million to a \$1 billion dollars to support the continued growth of our business.

Total inventory increased 13.9% for the end of the second quarter of 2015 compared to the end of the second quarter of 2014. As Ed previously mentioned, this planned increase was due primarily to earlier receipts of back to school merchandise and support for our outdoor business. For the third quarter, we anticipate inventory growth

to approximate sales growth. Second quarter net capital expenditures were \$55 million, or \$89 million on a gross basis.

Now, turning to our outlook for the remainder of fiscal 2015, we are raising our full year earnings guidance and now expect full year earnings per diluted share in the range of \$3.13 to \$3.21. We expect same-store sales to increase in the range of 1% to 3%, consistent with our prior guidance. Gross margin is expected to increase primarily driven by merchandise margin expansion and partially offset by occupancy deleverage.

SG&A is expected to deleverage as we invest in key marketing strategies as well as expenses related to bringing eCommerce on to our own platform. Year-over-year pre-opening expenses are expected to remain relatively flat as a percentage of sales. As a result of these dynamics, we expect operating margins on a non-GAAP basis to increase slightly year-over-year. Net capital expenditures for the full year are expected to be approximately \$245 million, or about \$365 million on a gross basis.

In 2015, we expect to open 44 new DICK'S stores, relocate seven DICK'S stores and relocate one Golf Galaxy store. We also remain focused on growing our Field & Stream concept and expect to open nine new Field & Stream stores this year.

For the third quarter of 2015, we anticipate earnings per diluted share in the range of \$0.45 to \$0.48. The growth in earnings will be driven by an expected consolidated same-store sales increase in the range of 1% to 3%, expansion in gross margin and a lower tax rate, partly offset by SG&A expense deleverage. During the quarter, we expect to open 27 new DICK'S stores, relocate five DICK'S stores, and open seven new Field & Stream stores.

In summary, we are pleased with our performance in the second quarter, confident we have the plans in place to deliver our 2015 guidance, and continue to successfully grow our business to drive long-term shareholder value.

This will conclude our prepared comments. We appreciate your interest in DICK'S Sporting Goods. Operator, please open the line for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you, sir. We will now begin the question-and-answer session. [Operation Instructions] And our first question will come from Kate McShane of Citi Research. Please go ahead.

Katharine McShane
Citigroup Global Markets, Inc. (Broker)

Q

Thank you. Good morning.

Edward W. Stack
Chairman & Chief Executive Officer

A

Hi, Kate.

Katharine McShane
Citigroup Global Markets, Inc. (Broker)

Q

My first question was on team sports. I just wondered if you could walk us through how you view this category in light of some of the participation declines we've seen in football and soccer, especially as we embark into the new fall season? And how do you mitigate some of this risk going forward?

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, Kate, we've seen some participation – loss of participation in football. We haven't seen that in soccer. And some of the participation in football has been a bit more difficult at the younger levels as opposed to getting up into the high school levels, so there's a little bit there, it's just more dramatic at the younger levels. But it feels that those kids who played football have moved to soccer or to fall baseball, and if you take out the soccer business from the World Cup, we're very pleased with our soccer business and our baseball business.

Katharine McShane
Citigroup Global Markets, Inc. (Broker)

Q

Okay. That's helpful. Thank you. And, if I could just ask a question on an update on your strategy to put more opening price points in the store. Where are we in terms of that strategy and are there still areas within the store that can benefit from this?

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, we're pretty pleased with where we are from an opening price point standpoint. We will be adding a couple of brands over the next – into the fall and into the fourth quarter and more into the spring brands that will be a bit more opening price point, such as SKECHERS, we plan to have a meaningful increase in our SKECHERS business going forward. But we're pretty pleased with where we are with the opening price points.

Katharine McShane
Citigroup Global Markets, Inc. (Broker)

Q

Thank you very much.

Edward W. Stack
Chairman & Chief Executive Officer

A

Sure.

Operator: The next question will come from Seth Sigman of Credit Suisse. Please go ahead.

Seth I. Sigman
Credit Suisse Securities (USA) LLC (Broker)

Q

Okay. Thanks. Hey, guys. Just wondering, if you could elaborate on some of the category trends in the second quarter. It looked like the business performed pretty much in line with your expectations overall despite some mixed commentary out there in the industry. So I was just wondering if you could talk to some of the categories that perform well, some categories that maybe are still underperforming, any color there?

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, Seth, as you know, we won't get to quite probably the granularity that you would like, but we continue to be happy with our – the athletic apparel business, that we talked about both on the men's side and in the women's side. The license business was not what it was last year, although we were pleased with the performance because of the meaningful World Cup business that we did in 2014. And we've been very pleased with the outdoor category and the golf business is getting better.

Seth I. Sigman
Credit Suisse Securities (USA) LLC (Broker)

Q

Okay. And then, just shifting gears, if you look at the promotional plans for the balance of the year, the topic of promotional activities come up a bit in recent quarters, Q2 seemed to be lower and pretty much in line with your plans based on your commentary and you were lapping some events last year. I think André you talked about merchandise margins improving in the back half of this year, which we saw this quarter. Just wondering if you could talk about the promotional plans and what you're seeing on the competitive landscape?

Edward W. Stack
Chairman & Chief Executive Officer

A

We feel that we don't think it's any more promotional than it was last year. We think that our inventory is in better shape than it was last year from a quality standpoint. We don't need to be as promotional on the golf business as that business has gotten better and the inventory has been cleaned up, so we're pretty confident with what our promotional cadence will need to be and is baked into our guidance.

Seth I. Sigman
Credit Suisse Securities (USA) LLC (Broker)

Q

Okay. Thank you.

Operator: The next question will come from Michael Lasser of UBS. Please go ahead.

Michael Louis Lasser
UBS Investment Bank

Q

Good morning. Thanks a lot for taking my question. On the just structural gross margin in the industry, you got a portion of the merchandise margin that you lost last year in this quarter back this quarter, but not all of it. So, based on your comments, you said the promotional activity was about equal to what it was last year. So are we just seeing that the merchandise margin rates in the broader sporting goods sector are just on decline and that's going to have a longer term impact on your business?

Edward W. Stack

Chairman & Chief Executive Officer

A

No, you got to be careful on how you take a look at this from a mix standpoint also. So some of the things that are lower margins that have done very well are the performance tracking products, those are higher ticket items, lower margin rates, so that's impacted the penetration of that product. And then, when I said the promotional activity was about what we expect it to be, that's really – I meant for the third and fourth quarter, we don't see anything really being able – having to drive that promotional activity more than what we think it is. And where we picked up some lack of promotional activity this year versus last year in this quarter was really around the golf business. We weren't nearly as promotional in golf this year as we were last year.

Michael Louis Lasser

UBS Investment Bank

Q

Were you promotional in other areas to drive the business?

Edward W. Stack

Chairman & Chief Executive Officer

A

No. No more than what we had been in the past. We picked up margin rate versus last year and we really weren't more promotional in others areas. We've got some other categories of merchandise that we're bringing in and testing that we think will be helpful. We've got a number of Jordan shops that are going to be going into the store that are really a test right now.

That's higher margin product. We've got a partnership with Polo – the Polo Sport brand that we'll have in 75 stores or so that will be higher margin rates and should be accretive to our earnings. Although it's only 75 stores right now, it's a test, and we expect that to be significantly more going into 2016 and 2017. But we continue to work the mix and try to drive that apparel business and footwear business in those higher margin categories.

Michael Louis Lasser

UBS Investment Bank

Q

And how deep is the Jordan test going to be?

Edward W. Stack

Chairman & Chief Executive Officer

A

We're going to start out – we're starting out with ten stores this fall and it will roll out if it goes well, and we expect it will, then there'll be a meaningful increase going into 2016 and 2017.

Michael Louis Lasser

UBS Investment Bank

Q

Okay. Thank you so much.

Edward W. Stack
Chairman & Chief Executive Officer

A

Sure.

Operator: And our next question will come from Matt Nemer of Wells Fargo Securities. Please go ahead.

Matt Nemer
Wells Fargo Securities LLC

Q

Good morning, and thanks for taking my questions. Could you tell me if the future Field & Stream locations are more likely to be side by sides? Or are you still planning to open stand-alones after you get through this 2016 class of stores?

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, we haven't made a final decision yet, but with the research that we've done and the first store that we've opened, and as we said, we plan to have four of these combo stores opened by the end of this year. We think the vast majority of these will be in the combo format. The customer, the research, the customers love the idea, the customers in Mobile, Alabama where we have it opened up have responded very positively. So I would expect the vast majority of them will be in the combo format.

Matt Nemer
Wells Fargo Securities LLC

Q

And you'll leave the stand-alones -- there's no plan to do anything different with those, the ones that you have will stay stand-alones?

Edward W. Stack
Chairman & Chief Executive Officer

A

Yeah. For right now, yes.

Matt Nemer
Wells Fargo Securities LLC

Q

Okay. Great. And then secondly, the higher credit facility, is that primarily general corporate use? Or is there an ability to use that to potentially increase the buyback or do some acquisitions?

Andr  J. Hawaux
Chief Operating Officer & Executive Vice President

A

Matt, it's for general corporate use, but it wouldn't preclude us from buying back shares with it and doing M&A activity with it. It's for general corporate purposes.

Matt Nemer
Wells Fargo Securities LLC

Q

Okay. Thanks so much.

Operator: Our next question will come from Simeon Gutman of Morgan Stanley. Please go ahead.

Simeon A. Gutman

Morgan Stanley & Co. LLC

Q

Thanks. Good morning. Quick question on back-to-school. DICK'S has always done a nice job around it and it's clearly embedded in the forecast. Without giving too much read into Q3, which you'll choose not to, can you give us just a sense of, I guess, anything with fall sports trending in markets where it's relevant or where back-to-school has begun yet?

Edward W. Stack

Chairman & Chief Executive Officer

A

Well, you're right. We don't talk about the quarter that we're in, but I can tell you embedded in our guidance we're optimistic about back-to-school. Couple of the things that we're enthusiastic about is the fashion trend in athletic apparel for back-to-school, in particular for men and women on the bottom's category. We're excited about the footwear business going to back-to-school, and the team sport business around the cleat business. So all in all, we remain optimistic about back-to-school. We're in better inventory shape than we were last year to begin the back-to-school season and we're pretty confident.

Simeon A. Gutman

Morgan Stanley & Co. LLC

Q

Okay. And then bigger picture, Nike, Under Armour, I think about 30% or so of brands, I don't know if you say it explicitly or they do, but it looks like the growth on that business has been decelerating over time. And it could be due to a bunch of things, certainly you're trying to diversify your revenue stream, you mentioned CALIA, some of it just could be law of large numbers. But I'm curious, what the right way to think about that is? Is the sell-through of that merchandise slowing or is that just law of large numbers and purposeful, given some of the focus on other categories or other brands?

Edward W. Stack

Chairman & Chief Executive Officer

A

We're continuing to grow both of those brands in our business and our stores. With the investments we've made in shops on both the Nike side and the Under Armour side, we continue to make investments in both of those brands around the youth apparel business and with some shops. And with what we're doing with Nike, we're really excited about it and they are too. Around these Jordan shops, we think there's still growth available in both of those brands.

Simeon A. Gutman

Morgan Stanley & Co. LLC

Q

Okay. Just to sneak in one last one. Just to clarify, back half of the year, gross margin guidance Q3, Q4, I don't know if you gave it explicitly, but I may have missed something. But what have you set on gross margin for the back half of the year?

Andr  J. Hawaux

Chief Operating Officer & Executive Vice President

A

Merch margin expansion and slight occupancy deleverage, but net-net we should see gross profit expansion.

Simeon A. Gutman

Morgan Stanley & Co. LLC

Q

Great. Thank you.

Operator: Our next question will come from Steven Tanal of Goldman Sachs. Please go ahead.

Stephen V. Tanal

Goldman Sachs & Co.

Q

Good morning. And thanks for the question, guys. Just wanted to follow-up on the color around promotions. We felt like we saw at least a lot more e-mails with offers, maybe not more offers in terms of – or bigger type of more impactful type promotions. But I'm wondering if you can sort of tie that out with the somewhat of moderation and online growth, which happened despite kind of an easier compare. Do you think those are related or is something else going on?

Edward W. Stack

Chairman & Chief Executive Officer

A

With regard to – we're very pleased with our online growth. I mean, we went from 6.3% of sales up to 7.3% of sales. We're really quite pleased with it.

Andrè J. Hawaux

Chief Operating Officer & Executive Vice President

A

So, Steven, this is Andrè. I think we also – let's not forget that both, not only did the brick and mortar business last year benefit from World Cup but as did our online business, so we were lapping a pretty significant Q2 number last year in online as well. So to Ed's point, we feel very confident in the way our eCommerce business continues to perform and this was an issue where we had a really, a very big quarter, we were lapping due to World Cup.

Stephen V. Tanal

Goldman Sachs & Co.

Q

Okay. Fair enough. And then on gross margin, you guys used to give a little bit more color. I mean it sounds like there's probably less of a headwind from shipping and freight which had been an issue. Could you sort of help us parse it out a little bit in terms of what merch margin was versus fixed costs as well?

Andrè J. Hawaux

Chief Operating Officer & Executive Vice President

A

Yeah. So what I'll do for you Steven is, I'll just stay at the highest level. So I'd say that our merch margin expansion was about 58 basis points and then we had some things moving up and down on a couple of the line items between merch margin and gross profit. The biggest factor that brought that number from 58 basis points down to the 47 basis points would be the occupancy deleverage and that's about as much granularity as we're going to provide.

Stephen V. Tanal

Goldman Sachs & Co.

Q

Okay. That's very helpful. Thanks. And just lastly on the buyback, sort of doesn't seem like anything else is in the guide, nothing done in 2Q. Care to comment on that at all?

Andrè J. Hawaux

Chief Operating Officer & Executive Vice President

A

No. I think we'll be consistent with what we said in the first quarter, or at least what I've said in the first quarter, which was, we've got \$150 million, you should bake that into your models. And if we do more between now and the back half of the year, we'll give that to you. So that's what we said in Q1, that's what we say in Q2.

Stephen V. Tanal

Goldman Sachs & Co.

Got it. Thanks a lot.

Q

Operator: The next question will come from Dan Wewer of Raymond James. Please go ahead.

Dan R. Wewer

Raymond James & Associates, Inc.

Thanks. So, Ed, in the last two or three quarters, when you break out the big growth online, it implies that your bricks and mortar same-store sales have been flat or slightly negative. I guess that was even before the tough comparisons with the World Cup, and I'm guessing that's probably the reason why the occupancy cost de-levered. But, going forward, are there any initiatives to drive faster bricks and mortar growth? Or is the future really predicated on the success of online?

Q

Edward W. Stack

Chairman & Chief Executive Officer

No. We've got – the online business will continue to be an important growth driver, as will the stores. And although we're not going to guide exactly what that number is, but yeah, we've got a number of initiatives in place to drive comp stores at the store level. So we believe the SKECHERS addition will be helpful. What we're doing with the Polo stores, at the Polo shops in 75 stores this fall we think will be helpful. We think that as we continue to go forward with these combo stores and being able to move the hunt, fish, and camp business out of the DICK'S stores into the Field & Stream side, giving us space to be able to invest a bit more heavily in the apparel business, the footwear business, will help those stores also. So, yeah, we've got a number of initiatives to drive that store productivity.

A

Dan R. Wewer

Raymond James & Associates, Inc.

Also had a question about gross margin rate in your online business, and the reason I'm asking is when you're waiting to check out in a retail store, you have all of the impulse items with the big margin rates that I'm assuming you're selling a fair amount of that product. So when you're customer is shopping online, they really are a hunter, they're probably not attaching those higher margin impulse items. I don't know if I'm right or wrong, but how would the margin rates compare on those two channels?

Q

Edward W. Stack

Chairman & Chief Executive Officer

We haven't provided that level of granularity, but we are extremely pleased with the profit margin and the profitability of where we are from an eCommerce standpoint, and it has grown, the profitability of that channel has grown significantly over the last several years.

A

Dan R. Wewer

Raymond James & Associates, Inc.

Q

And just one real quick question on Field & Stream when you launch your online capabilities. Any chance that you'll be able to start using the Field & Stream URL or will it have to remain Field & Stream shops to avoid, I guess, conflict the magazine?

Edward W. Stack

Chairman & Chief Executive Officer

A

Yeah. For right now it will have to remain that way.

Dan R. Wewer

Raymond James & Associates, Inc.

Q

Okay. Thank you.

Edward W. Stack

Chairman & Chief Executive Officer

A

Sure.

Operator: The next question will come from Paul Swinand of Morningstar, Inc. Please go ahead.

Paul Swinand

Morningstar Research

Q

Good morning and thank you for taking the questions as always. I wanted to ask about TaylorMade and the golf business. Obviously you're seeing a little more stability but you've also talked about TaylorMade being the industry leader and them being your biggest vendor. Is there anything that they are still maybe not back to normal on, and is there something that you can do together to still improve the business?

Edward W. Stack

Chairman & Chief Executive Officer

A

Well, I think you can see from their release, the Adidas release that the TaylorMade business is still not back to where it was. I think they've got more – this is probably grammatically not correct, they have more better competition out there right now. PING has done very well with the G30, Titleist has done very well with the 915 driver, Callaway with the Big Bertha product has done very well, so it's a more competitive environment out there on the golf side. But TaylorMade continues to try to improve that business. We actually have a -- we're going to be looking at their product for next year tomorrow and I'll have a better – I could answer that question better tomorrow than I can today.

Paul Swinand

Morningstar Research

Q

Okay. Great. I'll call you after tomorrow then.

Edward W. Stack

Chairman & Chief Executive Officer

A

Can't wait.

Paul Swinand

Morningstar Research

Q

I'm sure you'll be right on the phone. I wanted to ask about the Olympic sponsorships too. I know you're just the retail partner and, of course, Polo is still the actual official uniform. Can you give us any more color on what you actually have the rights to, and will – is there any opportunity from Polo to actually tie into Olympics or is that just the Polo Sport line is a pretty narrow line?

Edward W. Stack

Chairman & Chief Executive Officer

A

Well, it's Polo Sport, so we're not into -- it's the Polo Sport brand, and we're very excited about it. We think they've done a great job with that. We've been working on this for awhile with them, and we're pretty enthusiastic to get this up and running. As it relates to the Olympics, we're the official sporting goods sponsor. We get to use that from an advertising standpoint. And we're really enthusiastic about what we're doing with the Olympic hopefuls. These athletes that really still have to work and pay their way to get to the Olympics that they don't have a sponsor and we're trying to help them with flexible work hours and give them a job that they can train to get to the Olympics and still be able to feed themselves and feed their family. So we're really excited about this, and we've got a marketing campaign that we'll be launching shortly all around this we think will be very successful.

Paul Swinand

Morningstar Research

Q

So it's just brand marketing, there's not really any merchandise tie-in?

Edward W. Stack

Chairman & Chief Executive Officer

A

Yeah, there's no merchandise tie-in right now. No, we just wanted this to be a marketing event, and really try to help these young men and women who are trying to achieve their dream of participating in the Olympics and hopefully winning a medal.

Paul Swinand

Morningstar Research

Q

Great. Thank you very much. Best of luck.

Edward W. Stack

Chairman & Chief Executive Officer

A

Thank you.

Operator: The next question will come from Scot Ciccarelli from RBC Capital Markets. Please go ahead.

Scot Ciccarelli

RBC Capital Markets LLC

Q

Hey, guys, Scot Ciccarelli. Given your comments on the combo stores and some of the expected merchandise changes in the standalone DICK'S Sporting Goods stores, do you think you're actually space constrained in your existing DICK'S Sporting Goods boxes?

Edward W. Stack

Chairman & Chief Executive Officer

A

We definitely are based on what we could be doing in the women's business, the footwear business, the team sports business, we are definitely space constrained. We've been saying that for awhile.

Scot Ciccarelli

RBC Capital Markets LLC

Q

Okay. And then, secondly, regarding some of the – I think it was about a year ago you made some significant waiver changes on the golf business with the transition of the PGA pros. Have those changes had the desired impact on the profitability of that category, and how big of a difference do you think the service levels have been since that change?

Edward W. Stack

Chairman & Chief Executive Officer

A

I think we're back to the service levels that we're comfortable with and the profitability of the golf business is meaningfully more profitable than it was a year ago, not only based on the changes that we've made in the store, but also how we consolidated the operation in the back office here, so it's a meaningfully more profitable business than it was a year ago.

Scot Ciccarelli

RBC Capital Markets LLC

Q

Got you. All right, thanks a lot, guys.

Edward W. Stack

Chairman & Chief Executive Officer

A

Sure.

Operator: The next question will come from John Kernan of Cowen. Please go ahead.

John D. Kernan

Cowen & Co. LLC

Q

Hey, good mornings, guys. Thanks for taking my questions.

Edward W. Stack

Chairman & Chief Executive Officer

A

Sure.

John D. Kernan

Cowen & Co. LLC

Q

If we think about the long-term targets you recently put out, the 50 basis points to 70 basis points of gross margin expansion and then the 30 basis points to 60 basis points of SG&A leverage, how doable are those targets if comps stay around this 1% level? What type of comp do you think you need to really start accelerating towards those targets?

Andrè J. Hawaux

Chief Operating Officer & Executive Vice President

A

This is Andrè, John. I think what we laid out at the Analyst Meeting are the last targets. I mean, I think we feel relatively comfortable probably in that 2% to 3% range that we'd be able to get to some of the numbers. And again, I think we've – last couple of quarters, and we've been pretty clear about the headwinds that we faced as a business, but as we lap the World Cup here and as we go into Q3 and Q4, we feel very confident in our abilities to

deliver the targets that we laid out for this year, and clearly the ones that we shared with you all for 2016 and 2017. So we feel relatively confident in the numbers that we've laid out for you all.

John D. Kernan

Cowen & Co. LLC

Q

Okay. That's helpful. And then, you mentioned M&A as a potential opportunity. Can you just elaborate on what you'd be looking at there? Is there a specific category or channel that you'd look to expand into?

Andr  J. Hawaux

Chief Operating Officer & Executive Vice President

A

I don't believe we necessarily talked about M&A, but one of the things I did mention when the question was asked about what could you use the expanded facility for, I said it could be – it's for general corporate purposes, it could be for share buyback, and it could be for M&A, I believe that's the way the question was posed. So nothing imminent and nothing we certainly would discuss at this stage of the game.

John D. Kernan

Cowen & Co. LLC

Q

Okay. Thank you.

Operator: The next question will come from Sam Poser of Sterne Agee CRT. Please go ahead.

Sam Poser

Sterne Agee CRT

Q

Good morning. Thank you for taking my questions. When you're looking, the later back to school, it sounds like you feel pretty confident about it, can you give us some idea of with later Labor Day, the inventory levels, is that really the effect of the inventory levels? And given the guidance, I would assume you would expect to see a little bit of acceleration from second quarter in the same-store sales.

Edward W. Stack

Chairman & Chief Executive Officer

A

Yeah, so the later Labor Day is real. There's a lot of schools, especially in the northeast that go back Labor Day and Labor Day is a week later this year, so that's a big shift. And it is really around the inventory for back to school and what we've seen is an acceleration in our business on the outdoor category. So in order to keep up with the sales in the outdoor category and to be in a better position for back to school this year than we were last year has made a big difference. Last year there were some orders that were received late that when we started back to school, we weren't in as good an inventory position as we should have been last year, but we are this year, we've made those changes.

Sam Poser

Sterne Agee CRT

Q

Thank you. And then just a quick two follow-ups, you've given sort of the ex hunt, camp, fish, and golf comp, I wonder if you would give us that. And can you give us also some detail as what the product is – the Polo Sport product that's going into those shops? I mean, how we should envision what that's going to look like from a mix, from a product mix standpoint?

Edward W. Stack

Chairman & Chief Executive Officer

A

It's athletic apparel, the Polo product, so it's running shorts, it's athletic shorts, it's tanks, there are tech tees, it's fleece product, it's all very athletically-based and Polo is really – is very enthusiastic about participating in this and they came to us and asked us if we'd be interested in participating in this and taking a look at this and they've been terrific to work with and we're very enthusiastic about where this might go.

Andr  J. Hawaux

Chief Operating Officer & Executive Vice President

A

And Sam, we're eventually going to wean you all off this drug that you keep asking about what is it without golf and without hunt, but we're going to do it one more time. For DICK'S omni, instead of a 1.5% comp we would have been a 2.8% comp for this quarter, but, again I want to let our investors know that this is going to become less of a headwind for us and we're going to start to just stay very focused on the comps we normally give. But it would have been 2.8% versus 1.5%.

Sam Poser

Sterne Agee CRT

Q

And just a quick follow-up, lastly, that would have had something to do with the shift of that later back to school, there is a lot – you have to look at the two combined now because of the way the calendar is working these two quarters, I assume?

Andr  J. Hawaux

Chief Operating Officer & Executive Vice President

A

No, I think the way I'm answering your question was, what would our comps have been in this quarter ex the hunting and golf equipment, which is the same number we've talked about in the past. But, yeah, in fairness, yes, because the back to school is one week out later, you could argue that some of our sales that we didn't get in Q2, we'll be getting it in Q3 now as the Labor Day has moved and back to school has moved in some jurisdictions.

Sam Poser

Sterne Agee CRT

Q

Thank you very much. Continued success.

Andr  J. Hawaux

Chief Operating Officer & Executive Vice President

A

Yeah. Thank you, Sam.

Operator: The next question will come from Rick Nelson of Stephens. Please go ahead.

N. Richard Nelson

Stephens, Inc.

Q

Thanks. Good morning. The hunting category, if you could provide some color there as well as firearms and ammo and what you're thinking about kind of for the back half of the year?

Edward W. Stack

Chairman & Chief Executive Officer

A

Well, Rick, we won't get too granular on this category, but we're happy with our total outdoor business. The hunt piece of that has been behind the total outdoor business, and we still think there's a bit of hangover from those – last year when there was all that product was accelerated, but we're relatively confident that that hunt business will be relatively flat to next year and the total outdoor business will be up for the third and fourth quarter.

N. Richard Nelson

Stephens, Inc.

Q

All right. Thanks for that color. Also I like to ask you about golf, how that compares to Golf Galaxy comp, you obviously reported how the DICK'S stores performed in that category and how the profitability compares between the two concepts?

Edward W. Stack

Chairman & Chief Executive Officer

A

Well, we haven't broken out profitability between the two concepts, but the Golf Galaxy comps were slightly better than the DICK'S comp and both concepts are more – much more profitable than they had been a year ago driven by two things, a reduction of cost and an increase in margin rate, so although some people are still not happy about the golf business from a sales standpoint, from a profitability standpoint, it's much more profitable than it was a year ago.

N. Richard Nelson

Stephens, Inc.

Q

Okay. Great. Thanks for the color. Also, if I could ask one more about Texas and energy markets, if you're seeing anything different in those states?

Edward W. Stack

Chairman & Chief Executive Officer

A

Not as of right now.

N. Richard Nelson

Stephens, Inc.

Q

Thank you.

Operator: Our next question will come from Mike Baker of Deutsche Bank. Please go ahead.

Mike Baker

Deutsche Bank Securities, Inc.

Q

Thanks, guys. So, appreciate that you had a difficult comp versus last year and so that impacted the same-store sales, but your total sales growth is growing a little bit less than the industry which was putting up, 5%, 6%, 7% growth the last couple of months. Typically you've been at or even better than that, so do you think – is that just a function of the categories where you guys are heavier in or is there any kind of share loss or anything along those lines? Can you address that gap?

Edward W. Stack

Chairman & Chief Executive Officer

A

I guess, my -- I'm a bit confused. Where did you get the 5% number?

Mike Baker

Deutsche Bank Securities, Inc.

Q

From the retail sales numbers that come out every month NAICS, I think it's 45111 sale through Sporting Goods Stores.

Edward W. Stack

Chairman & Chief Executive Officer

A

Yeah, I don't think that's a comp number, and our total business was up roughly 10%.

Mike Baker

Deutsche Bank Securities, Inc.

Q

Right. Understood. But just historically, if you just look at the comp even without the new stores, your comp has been closer to the industry and there's been a little bit of a gap the last few months. My view is it's just a function of the categories you're in, but wondering if you guys kind of have any perspective.

Edward W. Stack

Chairman & Chief Executive Officer

A

I don't. I'm not sure we're comparing apples and apples, but if you wanted to, you take a look at the golf business isn't growing, but if you take a look at – if that golf business is in your numbers, I'm just not sure we're comparing apples-to-apples because it's not – the 5% number that you're talking about is not a comp store sales number.

Mike Baker

Deutsche Bank Securities, Inc.

Q

Right, fair enough. Okay. Understood. One other follow-up, if I could, some of these shifts in tax free holidays and the Labor Day we've talked about a little bit, but do you think that actually did impact the second quarter sales and would benefit the early back-to-school in the third quarter, in particular the tax-free holidays?

Edward W. Stack

Chairman & Chief Executive Officer

A

It affected it a bit, but – and it will help the third quarter, it will help with the third quarter a little bit, but it – we don't think it was really meaningful.

Mike Baker

Deutsche Bank Securities, Inc.

Q

Okay. Appreciate the color. Thanks.

Edward W. Stack

Chairman & Chief Executive Officer

A

Sure. Thanks.

Operator: The next question will come from Chris Svezia of Susquehanna Financial Group. Please go ahead.

Chris Svezia

Susquehanna Financial Group LLLP

Q

Good morning, everyone. And thanks for taking my questions. I guess, first just on – I'm intrigued by the SKECHERS brand coming into your stores. Maybe just a little more color, whether it's men's, women's, kids, are you doing anything special makeup related or is it just regular product categories, doors? Any additional color will be helpful.

Edward W. Stack

Chairman & Chief Executive Officer

A

Well, it's going to be men's, women's and kids. And we're not getting into special makeups right now, that's something that we'll talk about down the road, but we're pleased to be adding them to the assortment and we think that they'll be additive to our footwear business and our overall business.

Chris Svezia

Susquehanna Financial Group LLLP

Q

And is that all doors, just to clarify, or is it a slow ramp up?

Edward W. Stack

Chairman & Chief Executive Officer

A

It will be all doors in 2016.

Chris Svezia

Susquehanna Financial Group LLLP

Q

Okay. Fair enough. Profitability, just on the eCommerce side, I know you keep mentioning that the profits are up significantly. Any color, if you can just talk about from a margin perspective, I mean, from an operating margin perspective, I know it's still broadly below the company average, but is that every quarter as you continue to grow and make progress, are you narrowing that operating profit or EBIT margin gap each sequential quarter or year-over-year? How should we – and just any color about that?

Edward W. Stack

Chairman & Chief Executive Officer

A

We are, and we will expect to continue to do that. And when we flip over to our own platform, it becomes meaningfully more profitable to the point where it'll be almost the same, whether it's by online or in a store.

Chris Svezia

Susquehanna Financial Group LLLP

Q

Okay. And then last question I have is just – I know in the past prior to all the issues with golf and the markdowns and ammunition et cetera, you guys have always seeing merchandise margin improvement coming from things like the mix of business, more apparel and more footwear, private label, private brand and systems. I guess private label and private brand continue to grow. I think mix continues to be somewhat favorable. Any color about the systems piece if that continues to help you drive that product margin as we move forward?

Edward W. Stack

Chairman & Chief Executive Officer

A

Yes. We continue to work the systems. We think that there are some systems help that we can do from a planning and allocation of inventory. We think that as we move forward from an online standpoint that will help our profitability too as we direct ship from store product to stores where the product isn't selling. And although the

freight may be a bit more expensive, the markdown associated with that product would be – it will be accretive to us. So, yeah, there is still systems opportunity here to help drive margin rate.

Chris Svezia

Susquehanna Financial Group LLLP

Okay.

Q

Edward W. Stack

Chairman & Chief Executive Officer

And turn.

A

Chris Svezia

Susquehanna Financial Group LLLP

Okay. Great. Thanks. And all the best.

Q

Edward W. Stack

Chairman & Chief Executive Officer

Thanks.

A

Andr  J. Hawaux

Chief Operating Officer & Executive Vice President

Thank you.

A

Operator: The next question will come from Robby Ohmes of Bank of America Merrill Lynch. Please go ahead.

Rafe Jason Jadrosich

Bank of America Merrill Lynch

Hi, good morning. This is Rafe Jadrosich on for Robby. Thanks for taking our questions.

Q

Edward W. Stack

Chairman & Chief Executive Officer

Thanks, Rafe.

A

Rafe Jason Jadrosich

Bank of America Merrill Lynch

I just want to follow-up on the last questions on SKECHERS. Can you just talk about some of the trends you're seeing within footwear between running and basketball? And then are you seeing a pickup in casual athletic trends?

Q

Edward W. Stack

Chairman & Chief Executive Officer

So the basketball area is growing faster than the running area, for sure. There's definitely a trend in – a change in silhouette that's been going on for a little while now. The basketball silhouette is trending faster than the running silhouette. And then the casual athletic footwear piece is growing at a faster rate than the running silhouette also. So the growth drivers would really be basketball, the casual silhouette, followed by the running business.

A

Rafe Jason Jadrosich

Bank of America Merrill Lynch

Q

Are you seeing allocations improve kind of heading into back-to-school and kind of how are you positioned differently for this back-to-school versus last year? Do you just feel like your allocations are better in casual athletic?

Edward W. Stack

Chairman & Chief Executive Officer

A

Yeah. We feel that they are better in casual athletic. We've got a great relationship with the brands Nike, Under Armour, Adidas, and we're very pleased with what's going on right now.

Rafe Jason Jadrosich

Bank of America Merrill Lynch

Q

And last question, just – you closed three Golf Galaxy's in the quarter. Do you see additional opportunities through the back half of this year or maybe into 2016 to close additional stores?

Edward W. Stack

Chairman & Chief Executive Officer

A

Well, we'll take a look – as André said, those stores weren't making our hurdle rates. And as we take a look at these stores when they come up, as we've talked about for the last year or so, they're not making our hurdles that we'll close them and if they are, we'll renew them. And we've renewed a number of Golf Galaxy stores also.

Rafe Jason Jadrosich

Bank of America Merrill Lynch

Q

Okay. Great. Thank you.

Edward W. Stack

Chairman & Chief Executive Officer

A

Sure.

Operator: And ladies and gentlemen, this will conclude our question-and-answer session. I would like to hand the conference back over to Ed Stack for his closing comments.

Edward W. Stack

Chairman & Chief Executive Officer

I'd like to thank everyone for participating with us on our second quarter earnings call and look forward to talking to everybody for our third quarter. Thank you.

Operator: This concludes today's conference call. We thank you for your participation. You may now disconnect your lines.

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