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Dick's Sporting Goods, Inc. (DKS)

Q3 2018 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning and welcome to the DICK'S Sporting Goods' Third Quarter Earnings Conference Call. All participants will be in listen-only mode. [Operator Instructions] Please note this event is being recorded.

I would now like to turn the conference over to Jennifer Mejia, Manager of Investor Relations. Please go ahead.

Jennifer Mejia

Manager-Investor Relations, Dick's Sporting Goods, Inc.

Good morning, everyone, and thank you for joining us to discuss the third quarter 2018 results. On today's call will be Ed Stack, our Chairman and Chief Executive Officer; Lauren Hobart, our President; and Lee Belitsky, our Chief Financial Officer. Today's call will be archived for approximately 30 days on our Investor Relations website located at investors.dicks.com.

As a reminder, we will be making forward-looking statements, which are subject to various risks and uncertainties that could cause our actual results to differ materially from these statements. Any such statements should be considered in conjunction with cautionary statements in our earnings release and risk factor discussions in our filings with the SEC, including our last Annual Report on Form 10-K and cautionary statements made during this call.

We assume no obligation to update any of these forward-looking statements or information. Please refer to our Investor Relations website at dicks.com to find the reconciliation of non-GAAP financial measures referenced in today's call.

With that, I will now turn the call over to Ed.

Edward W. Stack

Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

Thanks, Jen, and good morning, everyone. This morning, we reported third quarter earnings per diluted share of $0.39 compared to GAAP earnings per diluted share of $0.35 and non-GAAP earnings per diluted share of $0.30 last year. Adjusted for the calendar shift due to the 53rd-week last year, our consolidated same-store sales declined 3.9% and our eCommerce business increased 16%.

As a percent to total net sales, the online business increased approximately 12% compared to approximately 10% in the same period last year. Revenue declined 4.5% to approximately $1.86 billion, including the impact of the calendar shift, which negatively impacted sales by $41 million.

Comp sales were in the range of our expectations for the quarter. As expected, sales were negatively impacted by the continued weakness in hunt and electronics, which contributed approximately 255 basis points to the comp decline. Despite these challenges, we have focused on driving profitable sales and managing our business to deliver higher earnings.

Merchandise margin expanded 213 basis points during the quarter as we benefited from the mix of the sales decline in low-margin hunt and electronic categories, fewer promotions and improved product cycle. This merchandise margin expansion drove an improvement in gross margin, which increased by 72 basis points.

Looking ahead, we will continue to optimize our assortment with the stronger emphasis on key items in a renewed focus on the enthusiast athletes. We remain encouraged by the improved product we're seeing from many of our partners and are optimistic about the pipeline into next year.

Our relationships with many of these partners have never been stronger and we will continue to work together to elevate the assortment and presentation at DICK'S. Our private brands continue to grow and are an integral part of our strategy to drive differentiation and exclusivity in our assortment.

We've seen great success in expanding our existing brands into new categories and that will be a priority going forward. We will also be launching new brands. Earlier this quarter, we launched the outdoor apparel brand, Alpine Design, and have been very pleased with the early success. We expect our private brands continue to deliver growth for us well into the future.

Finally, we continue to reallocate floor space to growth categories in key brands and adapt our profit offering to better align with the categories' our athletes' demand. Late in the third quarter, we removed virtually all hunt products from 10 DICK'S stores where the category underperforms and have replaced it with more compelling assortments in categories such as baseball, licensed products and outerwear. Though it's too early to discuss performance, we're optimistic these changes will better serve the athletes in these communities.

In closing, we are confident in the future of our business and believe we can strengthen our leadership position going forward.

I'd like to thank all of our team mates for their hard work and dedication to this company and for their upcoming efforts during the holiday season.

I'd now like to turn the call over to Lauren.

Lauren R. Hobart

President & Director, Dick's Sporting Goods, Inc.

Thank you, Ed, and good morning, everyone. As we enter the holiday season and look toward next year, we remain focused on providing an optimized omni-channel experience for our athletes through our three key strategic initiatives. These include improving our core execution, leveraging the power of our expert opinion to deliver a stronger merchandise assortment and presentation and increasing our productivity.

Beginning with improving our execution, we are delivering a better customer experience across our omni-channel platform. In stores, we've driven efficiencies within our processes, which have allowed our teammates to spend less time tasking and more time servicing our athletes.

We're also providing a stronger experience online by enhancing the functionality of the website and shortening our estimated delivery time. We're working to deliver eCommerce orders within two business days to the majority of our athletes in the future. To achieve this, we are investing significantly in our fulfillment and delivery capabilities, including the creation of dedicated eCommerce fulfillment centers in New York and California. The state-of-the-art facility that we're building in New York will be highly efficient as we invest in robotics to drive automation and reduce labor costs.

We also recently enabled all of our store-focused regional distribution centers to fulfill online customer orders. Additionally, we continue to leverage our proximity to our customers by shipping from all of our stores.

Next, we'll continue to deliver a stronger product assortment and leverage the power of our expert opinion to guide and inform athletes to select the right product for them. From a merchandising perspective, we continue to be pleased with how athletes have responded to our strike point presentations, which showcase key items in a very impactful way throughout the store. An example of this is the new YETI display that we've incorporated in many of our stores for the holiday season, which is a powerful presentation of that brand. Year-to-date, many of these strike points have resulted in strong double-digit sales growth.

In marketing, we're focused on building an emotional connection with our brand and driving traffic to our stores and our eCommerce site. We're currently running a holiday campaign featuring a family and their ping pong table through which we show that giving the gift of sport lasts a lifetime and actually has the power to bring families together.

We're also driving digital transformation across all aspects of our marketing, leveraging our vast Scorecard and Team Sports HQ datasets to drive traffic with athletes through timely and targeted messaging. And we continue to utilize our strong brand partnerships to drive growth through joint marketing efforts with many of our key vendors.

Finally, we remain focused on increasing our productivity. Across the company, we will have eliminated approximately $25 million of expenses by year-end, much of which has been reinvested in our strategic growth drivers. We will continue to make critical investments to support the long-term growth of our business, particularly in key growth areas such as eCommerce, Team Sports HQ and our private brands. Improving productivity to help offset some of these investments will be a major priority going forward.

In closing, we remain optimistic that the continued execution of these strategies will lead to stronger results and drive competitive advantage in the marketplace.

I will now turn the call over to Lee to review our financial statements and outlook in more detail.

Lee J. Belitsky

Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

Thank you, Lauren, and good morning, everyone. I'd like to start with a brief overview of our third quarter results. Adjusted for the calendar shift, consolidated same-store sales declined 3.9%, including a 16% increase in our eCommerce business. Transactions declined by 5.5% and average ticket increased by 1.6%.

Consolidated sales decreased 4.5% to approximately $1.86 billion. This reflects the impact of the calendar shift, which negatively impacted sales by $41 million or $0.10 a share in the quarter.

During the quarter, our best-performing categories included outdoor and athletic apparel, which combined for a mid-single-digit comp sales increase. And our private brands continued to comp positively with higher penetration as well. Notwithstanding these strengths, sales continued to be negatively impacted by double-digit declines in hunt and electronics, which contributed approximately 255 basis points to the comp decline as well as weakness in our outdoor equipment.

Specific to hunt, in addition to the strategic decisions we made regarding firearms earlier this year, the broader industry has decelerated and remains weak as evidenced by most recent national background check data. We believe this also contributed to the decline we saw during the quarter.

Gross profit for the third quarter was $523.6 million or 28.19% of net sales, a 72-basis-point improvement versus last year. Within gross margin, merchandise margin increased 213 basis points and was partially offset by occupancy deleverage and higher freight and shipping and fulfillment cost.

The merchandise margin expansion was primarily driven by a favorable merchandise mix, fewer promotions and improved product. Additionally, a favorable timing shift related to the expense recognition for changes we made to our Scorecard loyalty program last year also benefited gross profit by $7 million during the quarter. This shift in timing will negatively impact gross profit by approximately the same dollar amounts during the fourth quarter.

SG&A expense dollars were $468.7 million, a 1.5% decline from last year, as expense reductions more than offset strategic investments and higher incentive compensation. As a percent of sales, SG&A deleveraged 76 basis points to 25.24%. In total, we delivered third quarter earnings per diluted share of $0.39 compared to GAAP earnings per diluted share of $0.35 and non-GAAP earnings per diluted share of $0.30 last year.

Now, looking to our balance sheet, we ended the third quarter with approximately $92 million of cash and cash equivalents and $382 million of borrowings on our revolving credit facility. Additionally, our inventory levels increased by 0.8% in the quarter or down 1.2% on a shifted basis as our quarter ended one week closer to Thanksgiving than last year.

Turning to our third quarter capital allocation, net capital expenditures were $28.5 million. We repurchased approximately 3.1 million shares for $108 million at an average price of $35.29. These repurchases are indicative of our confidence in the long-term prospects for DICK'S Sporting Goods. We also paid approximately $22 million in dividends during the quarter.

Before we move on to our fiscal 2018 financial outlook, given the timing of our call as it relates to the holiday weekend, I'd like to briefly comment on our performance. As we reflect on the Thanksgiving shopping weekend, we are very pleased with our results both online and in our stores and we have incorporated the results of the weekend in our guidance.

For the year, we continue to expect full-year comp sales to decline by 3% to 4% and gross margin to be approximately flat versus last year. As a result of our strong earnings results in Q3, we are raising our full-year earnings per share guidance for the third time this year to $3.15 to $3.25, which represents a $0.25 increase to the high-end versus our original guidance that we gave this year of $2.80 to $3.

Our inventory is clean and well positioned as we enter the holiday season. And throughout the fourth quarter, we expect to build inventory versus last year to be ready for the important spring businesses. Upon fully executing this strategy, we expect inventory levels at the end of the fourth quarter will increase over last year. We'll provide fiscal 2019 guidance on our fourth quarter call in March.

And this concludes our prepared comments. Thank you for your interest in DICK'S Sporting Goods. And, operator, you may now open the line for questions.

QUESTION AND ANSWER SECTION

Operator: We will now begin the question-and-answer session. [Operator Instructions] The first question is from Mike Lasser of UBS. Please go ahead.

Michael Lasser
Analyst, UBS Securities LLC

Q

Good morning. Thanks a lot for taking my question. Lee, can you reconcile your comments about being pleased with your holiday shopping results online and in stores with your guidance that calls for basically a 3% to 4% comp decline in the fourth quarter? Were your comments about the holiday shopping period so far or at least the last week or so an indication that you're seeing performance that's in line with what you're guiding to for the fourth quarter?

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

So, our guidance that we gave for the full year coming out of the third quarter was negative 3% to 4% and we're sticking with that negative 3% to 4% for the full year. We are pleased with the results coming out of the weekend, but we did have very favorable weather for us, which helped drive some of our weather-sensitive businesses. Not sure, if that's going to hold up all the way through Christmas right now. So, we're pleased with the results, but there is a long way to go.

Michael Lasser
Analyst, UBS Securities LLC

Q

Okay. And my follow-up question is so hunting and activity trackers accounted for a little bit more than half of your comp decline in the quarter, what was driving the weakness in outdoor equipment and how did the footwear category perform?

And based on the answers to that and I know it's early, but is it reasonable to expect that the business can comp positive in 2019 in totality?

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

Well, with respect to the footwear business, the overall footwear business was about even for the quarter. Some of the equipment businesses, particularly outdoor equipment, the comp sales were down. Some of that driven a little bit by weather and probably some of it driven by some of the firearms' customers that we have also involved with the outdoor equipment and camp categories and so on that slowed that business down a bit as we started to see during the second quarter and into the third quarter as well.

Again, our view for next year really hasn't changed on that. Our apparel business has been gathering momentum. Footwear business is decent right now. And as we anniversary the hunt business, the changes we made there, the electronics business and it's more the Under Armour pieces from the early part of last year, our view isn't changed. And we think that the vast majority of these headwinds will diminish and we'll be in a better position to drive more favorable comps.

Michael Lasser
Analyst, UBS Securities LLC

Q

Okay. Thank you very much and good luck with the rest of the holiday.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

Thanks.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Thanks.

Operator: The next question comes from Simeon Gutman of Morgan Stanley. Please go ahead.

Simeon Ari Gutman
Analyst, Morgan Stanley & Co. LLC

Q

Thanks. Good morning, guys – and gals, sorry. My first question is in the second quarter, you left us with the impression that ex the hunt and electronics, and I don't want to say the brand, because I'm not sure you'll comment on it specifically, but I think ex Under Armour, the business was running somewhere in positive territory. I think that's what Michael was, I think, trying to get to.

Can you share a similar number? So, if we take – you take out the piece that hunt and electronic hurt this quarter and then maybe take out – if it's the Under Armour drag or not, what would the core categories have done in the third quarter and how does it compare on a run-rate basis?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Well, we said our comps were what they were and the hunt piece accounted for a big portion of that. We think the outdoor category, which is a spillover to the hunt business, is a portion of that too. We didn't call Under Armour out this time although the sales were still pretty soft in Under Armour. We had been able to plan for that and we offset the apparel categories in the third quarter. As Lee had talked about, we were mid-single-digit comps in the apparel categories between the outerwear categories and the athletic categories.

Simeon Ari Gutman
Analyst, Morgan Stanley & Co. LLC

Q

Got it. Okay. And would it be fair to leave with an impression that so the underlying business looks about the same and maybe slightly a little better if I include what happened over Black Friday, granted, it's a promotional weekend, but it sounds like you are pleased and I'm assuming the complexion of what you're pleased with shows that some of the things you're doing are gaining traction?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

That would be accurate.

Simeon Ari Gutman
Analyst, Morgan Stanley & Co. LLC

Q

Okay. And my follow-up, it's kind of similar to the last question, with the margin profile of the business looks pretty good, right, electronic and hunt will be almost out of the way, inventory looks okay. As we head into next year, Ed or Lee, do you feel stronger about the margin profile of the business or about the sales position?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

You know what, Simeon, we've never commented going forward. So, as Lee indicated, and I don't mean to dodge your question, I just want to be consistent with what we've done in the past, is that that we'll guide next year at our fourth quarter call. But as I said in my comments and Lauren said in hers, we're optimistic about our business.

Simeon Ari Gutman
Analyst, Morgan Stanley & Co. LLC

Q

No problem. Understood. Thanks and good luck.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Thanks. Okay. Thanks.

Operator: The next question comes from Chris Horvers of JPMorgan. Please go ahead.

Christopher Horvers
Analyst, JPMorgan Securities LLC

Q

Thanks. Good morning. So, a couple questions. First, on the hunt side, I guess how was the impact relative to where you thought, [ph] I'd give you – (19:34) the thought-process being – as that customer comes back, are they remembering the decisions and the publicity around the spring such that the business got worse or is that more a function of the business stayed the same, but maybe the industry got worse?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Well, the industry is difficult and you can see that from the [ph] mix checks (19:56) and some of the other things going on in the industry. But the comps were overall kind of in the zone of what we anticipated. So, let's put it this way, from a sales standpoint, we didn't have a surprise.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

Yeah. The one thing on the hunt side is, in the fall, the penetration in the hunt business is double in the fall of what it is in the spring. So, the third and fourth quarter about even and first and second quarter about even. It's about double the fall of spring. So, it has a bigger drag on the business in Q3 and Q4, just based on the size of the business.

Christopher Horvers
Analyst, JPMorgan Securities LLC

Q

Yeah. And then, presumably electronics went up in the fourth quarter – goes up in the fourth quarter on a mix basis relative to the rest of the year. So, does the combined hunt and electronics headwind – is that more significant in sort of – versus the 255 basis point that you just quoted on 3Q?

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc. A

A little bit.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc. A

Yeah. A little bit. I mean, yeah, it is a little bit more, but as we said, we bake that all into our guidance and we think it's still going to be negative 3% to negative 4% and we raised our EPS guidance.

Christopher Horvers
Analyst, JPMorgan Securities LLC Q

Got it. And then, the last piece is the SG&A trend, I mean if you look at the SG&A dollars relative to history sequentially year-over-year, this was a – sort of a – look like a big shift versus what we would have expected. So, was there anything unique in there? And is this the new trend that we should sort of build out our SG&A off of going forward?

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc. A

No. We've been working hard throughout the year to reduce our SG&A expenses and some of that involve like contract negotiations that have a little bit of a longer tail from when they negotiate to when it gets implemented, so on, but the short answer is we believe we're going into a new period of better expense management going forward.

And what we saw in the third quarter is a very strong performance on expenses. A little bit of it is driven by the calendar shift. In that, we have a little bit less payroll expense and a little bit less marketing expense due to the calendar shift, but a lot of it is due to better expense management overall and we expect that to continue going forward. There're not a lot of onetime items in there that will go away.

Christopher Horvers
Analyst, JPMorgan Securities LLC Q

Understood. Have great holiday.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc. A

Thanks.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc. A

Thank you.

Lauren R. Hobart
President & Director, Dick's Sporting Goods, Inc. A

Thank you.

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

Seth I. Sigman
Analyst, Credit Suisse Securities (USA) LLC

Q

Hey, guys. Thanks for taking the question. So, my first question is on the merchandise margins, up over 210 basis points. Obviously, you recouped a lot of the decline from last year, but the offsets this quarter through occupancy and fulfillment cost, it seemed to be greater than prior quarters. Now, some of that may be lower comps, but I'm just wondering, are you seeing greater pressure from eCommerce and fulfillment?

And then, as I look at over the next couple of quarters or so, as you lap the merchandise margin recovery that we saw this year, I'm just wondering, does that imply less upside coming from gross margin looking out? Thanks.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

Yeah. The one thing to consider in looking at the gross profit is, once again, it's the calendar shift, because we have – in Q3, due to the calendar shift, we kind of lost $40 million in sales and that's $40 million less that we can leverage against our occupancy expense and our fixed distribution expenses. So, that's a piece of it and that will continue to be a concern in the fourth quarter as well as we have another similar reduction in sales and we have 13 weeks against 14 weeks coming in. So, that's affecting it.

And the other piece of that is the higher penetration of eCommerce sales. So we went from about 10% penetration to 12%. That's a lower gross margin business for us, primarily because of the delivery expenses associated with the eCommerce business. So, it's a lower SG&A structure there and it's a higher cost of goods sold structure in eCommerce. So, as we do higher penetration of the business in eComm, that dynamic will change on the P&L as well.

Seth I. Sigman
Analyst, Credit Suisse Securities (USA) LLC

Q

And, Lee, can you just quantify how much did that week shift impact the gross margin specifically?

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

So, it was – $0.10 a share was the impact overall and that's mostly gross profit dollars, delivers a little bit SG&A in there, but it's mostly gross profit dollars.

Seth I. Sigman
Analyst, Credit Suisse Securities (USA) LLC

Q

Okay. And my follow-up question is around the reallocation of square footage that you're testing here. You're taking space away from outdoor. I know it's too early to talk about the sales lift, but I'm just curious, the categories that you are giving more square footage to, I guess, what is it about those categories? The demand trends in those category, is it stronger, did they not have enough space previously, are they high margin? Just how do we think about that strategy to reallocate square footage? Thanks.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Well, it's a little bit of everything. So, we talked about the outerwear business, we talked about the license business – the team license business and also the baseball business. We think there's a big opportunity from a baseball standpoint. That's a business that's growing pretty significantly, primarily at the expense of football.

As the football business has declined, the baseball business and soccer have picked that up. It is – in all of these businesses, there're significantly higher margin business than the hunt business.

Now, I just want to – it's a bit of semantics, but when you said you're taking business out of outdoor, we look at it a little different – we're taking business out of hunt, but the outdoor categories, if you take a look at camp, pedal sports that we're not taking space out of those categories, it's only the hunt category.

Seth I. Sigman
Analyst, Credit Suisse Securities (USA) LLC

Q

Got you. All right. Thank you.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Sure.

Operator: The next question is from Kate McShane of Citi. Please go ahead.

Kate McShane
Analyst, Citigroup Global Markets, Inc.

Q

Hi. Good morning. Thanks for taking my question. Just with regards to the fourth quarter and holiday, could you talk a little bit about your approach for promotions and traffic drivers, given that inventory is a lot tighter and the categories are a lot healthier versus last year?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Yes. We see that the – our inventory is in great shape. We don't see a needing to be as promotional. We've got more exclusive product. The product cycle is a terrific product cycle that's out there right now. So, we see this being much less promotional this year than it was last year, which is one of the reasons, we're able to continue to increase our guidance.

Kate McShane
Analyst, Citigroup Global Markets, Inc.

Q

Okay. That's helpful. Thank you. And then, with regards to footwear, it sounds like it was flat during the quarter on a comp basis. Was that in line with your plan, just given the level of newer innovation that you're seeing from the brand? And can you talk at all about how your full service footwear stores are doing compared to the rest of the chain?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Yeah. So, we won't give specific guidance on the full service footwear chains, but we're very pleased with that. We continue to gain momentum in those areas between access, et cetera. And the sales were primarily flat and primarily because our inventory was probably too low in the key back-to-school time. We have been under inventoried there and we're fixing that going forward into this quarter and into next quarter.

Kate McShane
Analyst, Citigroup Global Markets, Inc.
Q

Well, was that a function of just how you planned or was it because it is harder to get your hands on inventory, just curious, for footwear?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

It was a planning piece and a strategy piece, which has been rectified.

Kate McShane
Analyst, Citigroup Global Markets, Inc.
Q

Thank you.

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

Robert Ohmes
Analyst, Bank of America Merrill Lynch
Q

Hey. Good morning, guys.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

Hi.

Robert Ohmes
Analyst, Bank of America Merrill Lynch
Q

Ed, I was wondering if you could talk about the investment in the new eCommerce thesis and maybe walk us through how you think about Buy Online, Pick Up in Store versus shipping from store versus automated, putting up these two new facilities that are going to be very automated in our online-only. Just how do – maybe paint us the picture of where ultimately you see your omni-channel business shaking out?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

Well, I think that these are all important distribution points. The consumer, as we all know, wants their product how they want it, when they want it and delivered in the way that they want it. And this just gives us all the options to be able to do that.

We feel that the investments we're making from a omni-channel fulfillment center in New York and California will get us to the customer, because we have to do a better job of working on Speed to Customer.

And Lauren has been heading this up. So, I'm going to let her kind of answer the balance of the question here.

Lauren R. Hobart
President & Director, Dick's Sporting Goods, Inc.
A

Yeah. I would just say, Robby, we've been very focused on improving our speed and – Speed to Customer, we made small gains this year. But our goal is to get to the vast majority of our customers within two days. And to do that, we just need to make sure that we have the right inventory in the right place around the country. We're leveraging our entire store network and we're building these many fulfillment centers and larger fulfillment centers, so that we can take the speed question sort of off the table.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.
A

And let me just add one more thing to it. With these fulfillment centers, we're able to carry a larger assortment than what we carry in store. So, it allows us to keep orders together. They're more efficient than the stores. The automated facilities are more efficient. And as labor costs go up, that efficiency is going to be important to us.

And we expect to continue to have significant growth in our eCommerce business over time. And while we're not looking at real meaningful growth in our store count, we're already doing a tremendous amount of ship-from-store orders from our stores and we're concerned with keeping those stores in stock.

And as our eCommerce business continues to grow, we want to keep that kind of ship-from-store business relatively level within our stores, so we can stay in stock for the walk-in customers. So, we've got a number of reasons from speed, to quality delivery, to efficiency, to staying in-stock in stores, there're multiple reasons why we've got to add it – why we're adding a couple of distribution centers.

Robert Ohmes
Analyst, Bank of America Merrill Lynch
Q

That's helpful. And just a quick follow-up, when you look through Black Friday and Cyber Monday, any color on just the balance of – was digital much stronger or less strong relative to store traffic? Any kind of thought on how the shift is playing out?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

Well, I mean, we're very pleased with both channels, which we've said, but as Lee said, it was the coldest Thanksgiving in a long time, which really played into our strength, but we are pleased with both online and stores.

Robert Ohmes
Analyst, Bank of America Merrill Lynch
Q

That's great. Thanks so much.

Lauren R. Hobart
President & Director, Dick's Sporting Goods, Inc.
A

Thank you.

Operator: The next question is from Peter Benedict of Baird. Please go ahead.

Peter S. Benedict
Analyst, Robert W. Baird & Co., Inc.

Q

Hi, guys. Thanks. Ed, you mentioned improved product cycle a couple times here. Can you just expand on that? Where is that most pronounced? And then, talk about maybe the sustainability as you look out into next year. What are you seeing?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

I think there is some great – I mean, Nike has got some great product coming out. We're extremely pleased to with Nike on both the footwear side and the apparel side. We're pleased on the hardline side around golf with what we see with Callaway and TaylorMade, going forward, we're happy with what's going on with some baseball product we see. We're just in a pretty good product lifecycle. YETI is still doing very well for us. They've got some new innovation out there. Hydro Flask is doing very well.

So, we're just pleased with the products that we see out there today. And not to mention what we're doing with our own products, whether it'd be CALIA, what we're doing in the fitness products, we're going to be launching a new brand next fall, which we haven't really announced exactly what it's going to be, but we think it's going to be one of the biggest private brands we have. So, we're pretty enthusiastic about the product cycle out there both from the brands and what we're doing internally.

Peter S. Benedict
Analyst, Robert W. Baird & Co., Inc.

Q

Yeah. That's very helpful. So, on the space allocation comments you had there, two questions. One, the YETI set, is that something that is just a holiday increase or is that something that shift persists after the holiday? And then, are you considering removing hunt from more than just those 10 stores? Is there a certain basket of stores out there that that could make sense for as you look out into next year?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

So, the answer to the first question, on YETI, yes, this is something we plan to continue into next year. So, we bought it that way. We think our team, our merchandising team, store team, visual team, that's all worked together have put together we think probably the best YETI display in the country. And we're very pleased with that.

And as it relates to the 10-store test, we'll have to wait and see how the 10-store test does. Early reactions were pretty pleased, but it's too early to make any conclusions. But we are looking at a number of stores where the hunt business significantly underperforms and we'll assess whether we want to take it out and replace it with these other categories if that ends up to be a smart thing to do from a business standpoint.

Peter S. Benedict
Analyst, Robert W. Baird & Co., Inc.

Q

That makes sense. One last one for Lee. Just on the merchandise margin, as we think about the fourth quarter, you guys talked about probably a less promotional position here. There's been a favorable start to the season, presumably mix should be favorable. How should we think about the improvement merch margin relative to maybe the cadence we saw here in the third quarter? Could it be similar or should we not be expecting that much improvement?

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

I would not expect as much improvement in Q4 as we had in Q3, because Q3 last year, we were really – very aggressive markdowns. We weren't as aggressive in Q4 last year. So, the compare from merch margin perspective for us is a little more difficult against Q4.

Peter S. Benedict
Analyst, Robert W. Baird & Co., Inc.

Q

Okay. Great. Thanks, guys.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Thank you.

Operator: The next question is from Mike Baker of Deutsche Bank. Please go ahead.

Mike Baker
Analyst, Deutsche Bank Securities, Inc.

Q

Hi. You guys sound like you're doing a lot of investments in eCommerce. How does that impact your P&L next year? Is it going to be in SG&A impact? Would that preclude you from growing your margins next year?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Well, Mike, we're not giving guidance on the operating margins for next year. You're right, we're going to continue to invest in eCommerce, a lot of it is in fulfillments in the back half of the year, next year. So, those investments will be mostly in CapEx and then will be some in gross margin as we open up those buildings in the fall. Not much on the SG&A side.

Mike Baker
Analyst, Deutsche Bank Securities, Inc.

Q

Okay. And then, secondly, any update on what you're thinking regarding your Field & Stream stores, now that we are through another hunt season?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Well, we're not through the – so, excuse me, the specific answer to question is we haven't made any decisions yet and we are just – we haven't gotten through the hunt season. The hunt season is an important season in the fourth quarter too as big game season opens up in a lot of really high penetration hunting markets in the Northeast, here in Pennsylvania. So, we still have a little ways to go before we make a decision.

Mike Baker
Analyst, Deutsche Bank Securities, Inc.

Q

Okay. One more quick one. Any impact on the Red Sox winning the World Series? I have to get that one in there.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Yeah. Well, as a Yankee fan, I was disappointed, but, yeah, no really – it was not a real big impact. We were pleased with it, but Boston has won so many championships out of the last 15 years that it's getting to be expected. So, you don't get as big a jump out of Boston as we once did.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

Overall, though, I'd say a little bit smaller than Houston, but not material to the overall results for the quarter.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Yeah.

Mike Baker
Analyst, Deutsche Bank Securities, Inc.

Q

Okay. Appreciate it. Thank you.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Okay. Thanks.

Operator: The next question is from David Schick of Consumer Edge Research. Please go ahead.

David A. Schick
Analyst, Consumer Edge Research LLC

Q

Hi. Good morning. I just wanted to go back and sort of clarify or understand something a little bit better. You've talked a lot about baseball and the opportunity there and some of the product cycle things you like with a pathway into 2019. But, Ed, as you started the call, you said a renewed focus on the enthusiast athlete. I just want to go back to that, is that baseball or do you see that in other sports and would that be more of a top line or margin sort of mix opportunity?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Well, so we think it's a bit of both, a sales and a margin opportunity. And going back to this enthusiast athlete, we've kind of lost some of the product for that enthusiast athlete. And we're going back and reinvesting in that. In baseball, as an example, in 6 of the 10 stores that we redid taking hunt out, we put in a batting cage and HitTrax, which we're, off the First Tee so to speak, we're pretty pleased with. And it's a place where a young man or a young woman can come in and swing a bat.

It's similar to TrackMan in golf, where they can measure their bat speed, the ball speed coming off the bat, the angle of attack, gives them a tremendous amount of information about how they are hitting the ball and we can actually fit them with the best bat for them. And so an enthusiast athlete wants that product.

And these baseball bats are now – we're moving into some categories that are $300, $400, $500 for these bats. Where last year, we had a bat display of roughly 30 linear feet, we're going to have 80 linear feet of bats this year, a more enthusiast display of baseball gloves with the A2000, Heart of the Hide.

In the outdoor category, we're going to have – from a kayaking standpoint, we're moving our – the quality and the enthusiast level kayaks where we'll have kayaks that will be in that higher price points and we've kind of reduced the investment in the marketing in these better products for the enthusiast athlete and we're making a big change in that going forward into next year, which is why when Lee talked about the inventory at the end of the fourth quarter would be above last year, that's because we're making these investments in this product to service this enthusiast athlete going forward and we want to be ready for spring.

David A. Schick
Analyst, Consumer Edge Research LLC
Q

That's very helpful. Would some of those technology, sort of in-store experiences, would you think about those in soccer and basketball as well? I know some of that's out there.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

So, I'm not sure we would in basketball right now, but in soccer, yes.

David A. Schick
Analyst, Consumer Edge Research LLC
Q

Okay. Thanks.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

Sure.

Operator: The next question is from Brian Nagel of Oppenheimer. Please go ahead.

Brian Nagel
Analyst, Oppenheimer & Co., Inc.
Q

Hi. Good morning. Thanks for taking my question. So, I wanted to focus on sales as well. And, Ed, just wonder, if sales – at least headline sales numbers have been weak for a while, [ph] it sounds like as you did (40:19) articulate there's a lot of moving parts here, particularly with categories like hunt and electronics. But as you look deeper at the numbers, how would you track it from a market share standpoint in some of your key categories?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

We actually think that we're picking up market share in a lot of the categories. We think we're picking up market share in golf in the Team Sports category, because there's a number of ones we think we're picking up market share. We're pretty enthusiastic going forward.

Brian Nagel
Analyst, Oppenheimer & Co., Inc.
Q

And then, just maybe as a follow-up to that, I mean overall in the competitive environment, clearly there's been a pretty significant shake-out within your segment and maybe we're lapping past that now, but – how do you view competition right now either from a physical store standpoint or what's happening with the manufacturers and some of their direct-to-consumer efforts? Thanks.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

I'm not sure I understand the question, Michael (sic) [Brian] (41:20).

Brian Nagel
Analyst, Oppenheimer & Co., Inc.

Q

Well, no, it's – I guess let me ask maybe quick. How [ph] do you view competition in this space (41:25) right now? I mean competition has been an issue for a while. It seems like maybe its subsiding. I mean [ph] do you overall view it as (41:33) the competition less severe at this point?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Well, I think it's better competition. So, I mean, obviously, what the brands are doing and I'll come back to that, but the brands are more competitive. And what Amazon is doing is certainly they're clearly our number one competitor. And then, you've got Academy and a few people like that. So, the competition has gotten maybe less competitors, but the competition is better than it was in the past.

I think the piece with the brands is somebody will crab at me about this, but I think the brand as competitors is a bit overblown as it relates to us and a few other key retailers, because the brands are very helpful in trying to drive our online business, they're very helpful to let us know what's going on with their business online, we share information. I wish the brands weren't going direct, but they're also very helpful trying to drive our business online. And there is a real partnership there with the vast majority of the brands.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

Also, Brian, I want to just reflect a little bit more on your market share question. With respect to the apparel business being up mid-single digits this quarter, we're in a pretty strong apparel cycle overall and some of our competitors have been pretty strong in that space as well. But I think we're at least holding our own in the apparel space right now and we're doing that overcoming kind of the Under Armour situation that we're dealing with. So, we think we're doing well on the apparel front.

Brian Nagel
Analyst, Oppenheimer & Co., Inc.

Q

Right. Thanks for all the clarity. Appreciate it.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Thanks, Brian.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

Thanks.

Operator: The next question is from Tom Nikic of Wells Fargo. Please go ahead.

Tom Nikic
Analyst, Wells Fargo Securities LLC

Q

Hey. Good morning, everyone. Thanks for taking my questions. I just wanted to follow-up on Under Armour a little bit. Ed, on the last couple of calls, you've spoken about how you feel, like the pipeline coming out of Baltimore is a little bit better. Could you just sort of give us any updates on your thoughts on the Under Armour pipeline and also, your thoughts around channel differentiation for that brand and if you think that you're seeing better differentiation there? Thanks.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

I think we're seeing better going forward as it relates to us. We've worked with Under Armour. We think things with Under Armour in our stores are getting better. We are enthusiastic about some of the plans we've got with Under Armour going forward. And we think the vast majority of this headwind will be behind us as we come out of the first quarter of next year. So, we're enthusiastic about some meaningful parts of the Under Armour business.

Tom Nikic
Analyst, Wells Fargo Securities LLC

Q

All right. And one follow-up just on the cost side. Obviously, retail wages, there's been a lot of inflation there in the last couple of years and how should we think about wage inflation for you guys and store staffing levels and just general sort of labor costs for your business?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

There is wage pressure for sure and it's going to continue. We've got that baked into obviously what we're talking about for the fourth quarter and we're layering it into our budget for next year, which we'll talk about at the end of the quarter. But there is definitely wage pressure.

Tom Nikic
Analyst, Wells Fargo Securities LLC

Q

All right. Thanks very much. Best of luck for holiday.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Thank you.

Lauren R. Hobart
President & Director, Dick's Sporting Goods, Inc.

A

Thank you.

Operator: The next question is from Omar Saad of Evercore ISI. Please go ahead.

Omar Saad
Analyst, Evercore ISI

Q

Thanks for taking my question. Wanted to ask couple questions on digital. Last year, you announced the new Technology Officer, Paul Gaffney, to lead the tech efforts. Would love an update on kind of some of the changes and opportunities he's made and opportunities he sees, changes you guys have made. I think recently you've re-launched the new web platform. Maybe help us understand what some of the new capabilities are there? How you're tied into the app? Maybe just to build deeper kind of update on what's going on digitally for you guys. Thanks.

Lauren R. Hobart
President & Director, Dick's Sporting Goods, Inc.

A

We are incredibly pleased with how we're doing from a digital standpoint both from a technology standpoint in terms of – we mentioned last Q4 that we were digesting the new platform, it had launched in January of last year and at peak volumes in Q4, we had some issues last year.

The technology team under Paul's leadership has worked incredibly hard to make the site incredibly resilient and stable, which is a gift that keeps on giving. And then in terms of speed of the site experience, checkout has been approved. And we think we have been much more runway to go still to make the site an even better customer experience.

As we mentioned, we are working on the fulfillment aspect of it. The entire company is working on a digital-first approach. And I would say that that's beyond technology. It's in the eCommerce team, it's in the marketing team, where we are still – we're spending significant amounts of our marketing investment in the digital channels to help drive both brick-and-mortar and the eCommerce site. So, digital is an enormous focus and we're very pleased with the progress we've made.

Omar Saad
Analyst, Evercore ISI

Q

Okay. That's helpful. And one follow-up if I may. Any update on The Rock shoe? We've seen Under Armour doing a lot of content in the digital ecosystems talking about that shoe. I think it's exclusive to you guys, but maybe you could just give us an update how you're thinking about that product.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Well, so we're not going to give specific to a particular product like that, but we are pleased with that and we think that there is a lot of runway in that shoe and The Rock.

Omar Saad
Analyst, Evercore ISI

Q

Is it exclusive, Ed?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

It's not completely exclusive. There is some other people that have it. I mean Under Armour has it on their site, but we're a big player in that.

Omar Saad
Analyst, Evercore ISI
Q

Got you. Thanks. Good luck for holiday.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

Thank you.

Operator: The next question is from Scot Ciccarelli of RBC. Please go ahead.

Jonathan Livers
Analyst, RBC Capital Markets LLC
Q

Hey. Thanks for taking my question. This is actually Jonathan Livers on for Scott this morning. Given the CapEx guidance has come down significantly, I was wondering if you could give us some color around maybe your store strategy 4Q and then just generally how you're thinking about it going into next year? Thanks.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.
A

Well, we did bring down the CapEx forecast from $225 million to $165 million. There's about $40 million of timing differences in there, where we thought we were going to get to some of those items kind of in the latter part of the fourth quarter and they now look like they're going into the first quarter and it's about $20 million of savings there.

With respect to new store openings, we had guided some time ago that we will continue the slow pace of new store openings. We expect that to continue into next year. So, most of our CapEx going into next year are going to be around eCommerce fulfillment technology and more general technology around the eCommerce space as well as some standard kind of refixturing programs that we do in our stores.

Jonathan Livers
Analyst, RBC Capital Markets LLC
Q

Got you. That's very helpful. And just a quick follow-up, if I could, on the point you're making around eCommerce fulfillment. Is there a scenario in the future where you perhaps are no longer shipping from stores for eCommerce orders or is there always going to be some mix? Thanks.

Lauren R. Hobart
President & Director, Dick's Sporting Goods, Inc.
A

Yeah. This is Lauren. We believe we will always had some mix and getting that balance right is important. It is allows us to open up our entire inventory to all of our customers and maximize availability. So, it's not something that we see going away.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.
A

Also, when we get into the peak holiday seasons, it allows us to maintain the shorter shipping windows as we get these big surges of business between Thanksgiving and Cyber Monday that it's hard to handle out of a couple of buildings. So, having all 800 location shipping allows you to get the orders to the customers faster.

Jonathan Livers
Analyst, RBC Capital Markets LLC

Q

Understood. Thank you very much. And good luck this holiday season.

Lauren R. Hobart
President & Director, Dick's Sporting Goods, Inc.

A

Thank you.

Operator: The next question is from Sam Poser of Susquehanna. Please go ahead.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

Thank you for taking my question. Most have been answered. I do want to ask you about your sort of like how the – how you're handling in apparel some of the more fashion versus function apparel, because a lot of these sort of more heritage brands are coming back, but wanted to see if you're participating in that?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

We are with some. So, I mean the Champion brand has been great. We've got the Champion brand and it's been terrific. We think that will grow pretty significantly going forward. We've got some work that we're doing with Puma. I know that we're not doing a lot right now, but the team is talking with Fila.

So, there is a fashion component to this that we will play in. We'll be careful with the fashion side. We're really focused on that authentic enthusiast athlete as we've always been, but that athlete is is looking for a little bit more fashion product that we got it from those brands. And then, Nike, adidas, we are really happy about the assortment we see coming in from Nike going forward.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

Thank you. And then, just two other housekeeping, what share count do you have sort of assumed in the guidance now? And secondly, what's the tax rate that you have [ph] assumed in guidance (51:41)?

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

Hold on a moment.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Sam, can we follow up with you on that in a call a little bit later?

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

Sure that. Thank you.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Yeah. No problem.

Operator: Your next question is from Joe Feldman of Telsey Advisory Group. Please go ahead.

Joseph Isaac Feldman
Analyst, Telsey Advisory Group LLC

Q

Yeah. Hi, guys. Good morning. Wanted to ask you about tariffs, I guess. Are you seeing any impact there or how are you planning for it? And is that why inventory – did you accelerate some inventory because of the constraints on the freight coming overseas? Or anything related to that would be helpful.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

Yeah. There's a little bit of accelerated freight coming in for January. It's not really much of anything to speak of for the November quarter. As of right now, the tariffs are concentrated in our hardlines areas that we've got. And there's been some devaluation of the yuan since tariffs have announced and we're going to attack in a number of different ways.

We've got some – a little bit better pricing, we can get out of China to offset some of that and we'll be negotiating with our vendors to absorb some of that and some of it will come through and we'll have to, in some cases, raise our prices to our customers along the way. But that will play out over the course of the year next year and it's kind of hard to determine what impact it will have right now on sales or profitability at this point.

Joseph Isaac Feldman
Analyst, Telsey Advisory Group LLC

Q

And can you remind us what your exposure is to the current tariffs?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

So, we haven't specifically guided to that. A lot of it has to do with how our brands are going to handle it. We, obviously, know about it with respect to our own private brands and what we've got there and it's not based on the tariffs that are in place right now. It's not meaningful for next year for us, but again it's going to come down to the negotiations with the brands in the factories going forward to determine the impact.

Joseph Isaac Feldman
Analyst, Telsey Advisory Group LLC

Q

That's helpful. Thanks. And if I could follow-up with one another one, given what you've been removing with the hunt category and I understand the expansion in some of those other baseball and Team Sports or license apparel. And maybe too early to say this, but are you guys rethinking the box at all, like in terms of the size of the box or are you still pretty comfortable with it and maybe you just flex the different categories to still fill it and you still get the productivity that you would normally get out of that box?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

We feel pretty comfortable with the box that we have – the size of the box we have right now. And as we take out the hunt piece and test this, there were categories that we felt were constrained such as the Team Sports area, baseball is one in particular. The license business is another category that we feel that we've got a big upside with that we just haven't been able to provide enough space to.

In key cold weather markets, northern markets, that outerwear category, we think we've got the ability to expand there and provide a better offering to the athletes in that category. So we're – to answer your question, we're comfortable with the size of the box.

Joseph Isaac Feldman
Analyst, Telsey Advisory Group LLC

Q

Great. Thank you, and good luck with this holiday period. Thanks.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Thank you. Thank you.

Operator: The next question is from Matt McClintock of Barclays. Please go ahead.

Matthew McClintock
Analyst, Barclays Capital, Inc.

Q

Hi, yes. Good morning everyone and thanks for taking my question. Ed, I was wondering if we could focus on CALIA for a second, because it's been a couple of years or several years now of pretty positive comments that you've given to the brand and as we look forward now after several years of that type of growth, what are the main growth drivers for the brand? Is it expanded assortment? Is it new innovation? Is it better style or is it just to increase brand awareness? Thanks.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

There's a whole bunch of – we continue to be really excited about CALIA and as – the Genesis of CALIA was really from Lauren and her team, I'm going to let her kind of answer that question for you.

Lauren R. Hobart
President & Director, Dick's Sporting Goods, Inc.

A

Yeah. CALIA has been an incredible success story and we have been talking about it and we keep finding new ways to grow the brand. It's been getting into new categories. We have plans in the future to keep going in terms of expansion of the type of product that we drive and we think the brand relevancy also just continues to grow and as a heavy user of the product myself, the product itself is beloved by people who wear it and so it's doing its own job of just driving incredible loyalty. You should give it as a gift and you'll see, this is a fabulous product, this is a fabulous product.

Matthew McClintock
Analyst, Barclays Capital, Inc.

Q

Thank you very much for the color.

Lauren R. Hobart
President & Director, Dick's Sporting Goods, Inc.

A

Yep.

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

John Kernan
Analyst, Cowen & Co. LLC

Q

All right, good morning guys. Thanks for squeezing me in and taking my questions.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

No problem.

John Kernan
Analyst, Cowen & Co. LLC

Q

Lauren, can you talk to the driver – what would drive the operating margin on the eCommerce business higher and more in line with stores at this point? We know its gross margin dilutive. I'm just wondering as you make investments in fulfillment and other areas, is there an opportunity for this rapidly growing part of your business to become more profitable?

Lauren R. Hobart
President & Director, Dick's Sporting Goods, Inc.

A

Yeah. There absolutely is and we're working on profitability. Part of the reason for taking the site in-house was that we control our experience and the other part was that we get much more leverage as we grow and so we are very focused on eComm profitability. There are shifts as we mentioned earlier in terms of where expense goes into gross margin versus SG&A, but overall we look at this business as highly profitable, increasing in profitability and we do maintain a really indifferent look when we look between store sales and eComm sales, we don't have a preference for where they come in.

John Kernan
Analyst, Cowen & Co. LLC

Q

Okay. And then, Lee, just a follow-up on the CapEx question, it sounds like there's some shifts out this year into next year. But can you help us understand what you think is a steady run rate or maintenance CapEx level going forward as store growth slows? Because obviously, going from where you were last year to where you're guiding this year, it's a big boost of free cash flow.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

Right.

John Kernan
Analyst, Cowen & Co. LLC

Q

You could be generating almost over $400 million of free cash flow this year. So I'm just wondering is this CapEx run rate going forward more sustainable?

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.
A

Yeah, it's probably a little bit low this year, but it's much closer to this year's levels than certainly last year.

John Kernan
Analyst, Cowen & Co. LLC
Q

Got it. All right thank you.

Operator: The next question is from Adrienne Yih of Wolfe Research. Please go ahead.

Adrienne Yih
Analyst, Wolfe Research LLC
Q

Good morning. Thanks for taking my question as well. I was wondering if you could talk about the real estate portfolio, actually just in general rents over the next year. How many lease actions do you actually have coming up over the next three years? So just trends on that line item? And then similarly, with regard to cost inflation on freight pressure, are you seeing during the fourth quarter and then heading into first quarter increases in shipping and air rates? Thank you very much.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.
A

Okay. So, we have 80 to 100 store leases coming due each year that we have options on. So, we have a very aggressive process to try to manage those costs down. And with that many stores, we've got a lot of opportunity there.

With respect to freight rates, we have seen meaningful increases in freight rate, we do very little in air freight, so it really doesn't impact us much, but we have seen increases, particularly, on the inbound freight side not so much on the outbound side, plus we've got dedicated fleets there. But the inbound we have experienced those increases – expect those to carry into next year.

Adrienne Yih
Analyst, Wolfe Research LLC
Q

Okay, great. Thank you very much. And then really quickly, what percent of orders are currently on the free two-day shipping?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

A significant amount, we haven't guided to that exactly.

Lauren R. Hobart
President & Director, Dick's Sporting Goods, Inc.
A

Yeah, a large majority.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

Very large, more than half.

Adrienne Yih
Analyst, Wolfe Research LLC

Q

Okay, great. Thank you very much and best of luck.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Thank you.

Lauren R. Hobart
President & Director, Dick's Sporting Goods, Inc.

A

Thank you.

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

Thanks.

Operator: The next question is from Jim Duffy of Stifel. Please go ahead.

Peter Clement McGoldrick
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Hi, this is Peter McGoldrick on for Jim. Thanks for taking my questions. I was curious on the traffic and ticket breakdown, are you able to give any further detail between the split between retail and eCommerce? You had mentioned being pleased with store traffic, is there any sequential improvement here?

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

We haven't broken that down in the past, so we won't be doing that today either.

Peter Clement McGoldrick
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Fair enough. How about on marketing, as you invest in digital marketing as a traffic driver, does that primarily benefit traffic to the site or is that a store traffic driver as well?

Lauren R. Hobart
President & Director, Dick's Sporting Goods, Inc.

A

Absolutely, we look to digital to drive both traffic to the site and to the stores and we measure all of our returns on an omni basis. So, people – at different points in the shopping funnel are doing different things in digital and some of them are doing research that ultimately ends up in a store purchase and we are very focused on the omni return of that channel.

Peter Clement McGoldrick
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Okay. Thank you. And if I could just for one more on the merch margin expansion, you called out improved products as a driver and could you give any further detail on this excluding hunt and electronics? Is this is a function of pricing against easier compares or is this something that you can build on in the future?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

We think the product cycle is very good going forward, so we think it's something we can build on going forward.

Peter Clement McGoldrick
Analyst, Stifel, Nicolaus & Co., Inc.
Q

All right. Thank you.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

Sure.

Operator: The next question comes from Camilo Lyon of Canaccord Genuity. Please go ahead.

Pallav Saini
Analyst, Canaccord Genuity, Inc.
Q

Hi, thanks for taking our questions. This is Pallav Saini on for Camilo. Ed, since you've launched your own outdoor brand, have you shifted any floor space between the brands based on the number of stores this brand is available in and the initial positive response that you've seen from the consumer?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

Yeah, we're pleased with the response we've seen so far. This is primarily in some – we didn't launch this to all stores, it's in a limited number of stores to test, I'm not sure exactly how many, but roughly 100 or so – 90 to 100 stores or so. And they were mostly bigger square footage stores. So, it was easy to kind of move those in there. We're very pleased with it and we think it'll be a bigger part of our business going forward to next year.

Pallav Saini
Analyst, Canaccord Genuity, Inc.
Q

Thanks for that. And my second question is on the private-label brand launch you mentioned earlier for next year, can you provide any more color on – I think you mentioned fitness. Can you provide any more color on the category and the type of product that you'll be launching?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

Not at this time, but we'll talk more about it either at the first quarter call or second quarter call.

Pallav Saini
Analyst, Canaccord Genuity, Inc.
Q

Thanks and good luck for the rest of the holiday season.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

Thank you. Thank you.

Operator: The next question is from Chris Svezia of Wedbush. Please go ahead.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Hey, good morning, everyone. Thanks for taking the questions. I guess, first just on the – just to clarify the electronics category. You still anticipate being out of that at the end of the fourth quarter, so going into next year it's no longer a headwind. Is that true?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

It'll be really small. But the headwind will subside pretty significantly.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay. I guess, Lee, for you, just on the merchandise margin, just to clarify something. The mix component related to the declines in hunt and the declines in electronics, can you – any way you can quantify that more specifically as to what's that doing to your merchandise margin or maybe rank and priority? Or just maybe how we isolate that one specific dynamic against the other buckets in merchandise margin?

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

I mean that's an important aspect of the growth in merchandise margin for us. Between that and reduced promotions, that's really what's driving merchandise margin.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

When we talk about last quarter, those – that hunt category is roughly 1,700 basis points below the company average.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay. So it's fair to say it's a pretty significant piece of the merchandise margin improvement so far this year?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

I don't know if I would say a pretty significant piece, but it's meaningful, but...

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

We've had a lot – we've had margin expansion in a number of categories that are go-forward categories.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Right. Okay. And last question I have is, just – I know there's a lot of moving pieces here, but when you sit back and look at the leverage point in the business. I remember back in the day, it used to be 10% sales growth, you can leverage occupancy, I know a lot has changed here, but what kind of metric or how should we look at the leverage point on occupancy and SG&A? Is a 2 comp positive? Is it 1 comp, or just kind of what metric or how we should think about that as we go forward, that would be helpful?

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

It's – you can see the SG&A expenses were down for the quarter. I wouldn't expect them to be down every quarter, but it's much – I would say, we're in that low-single-digits range.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

So low-single-digit positive comp, you begin to leverage the occupancy and SG&A of the company in total, is that fair?

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

The company in total, yeah.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay. All right. Understood. Okay. Thanks very much and all the best around holiday.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

A

Thank you. You too.

Operator: And the last question today is from Steve Forbes of Guggenheim Securities. Please go ahead.

Steven Forbes
Analyst, Guggenheim Securities LLC

Q

Good morning. I wanted to focus on the implied 4Q gross margin. Since you mentioned flat for the year, so maybe if you can just speak to the magnitude or the change, right, and some of the pressures you anticipate offsetting what we think will be ongoing merchandise margin expansion in the 4Q quarter, any color on that would be helpful?

Lee J. Belitsky
Executive Vice President & Chief Financial Officer, Dick's Sporting Goods, Inc.

A

Well, what we've got in the fourth quarter is, we have one fewer week and we have a calendar shift, both working against us. So we have about $145 million less in sales due to those two factors, to offset the fixed cost and rent and within our distribution network as well. So that's a significant drag for us. And then, we obviously were forecasting comps to be down as well, which are kind of deleveraging. And the last piece is the eCommerce business becomes a much bigger part of the overall business for us in the fourth quarter and that has a lower margin profile primarily due to the delivery expense. And all those three factors work against us in a much bigger way in the fourth quarter than they did earlier in the year. It's a matter of fact the calendar shift was favorable for us in the first six months of the year. That was favorable from a fixed cost leverage perspective with regard to gross profit, so that's turning around with the fourth quarter being the biggest item. So those are the two – those are the main drags that we've got there.

And then the last piece of it is the – working against us is the change in timing of the Scorecard Rewards, the expiration of the points there, so we picked up about $7 million of merch margin there in Q3 and that's going to reverse in Q4 and be about $7 million going the other way. So we've got a lot of kind of – I'm going to call them calendar and sort of structural headwinds that are kind of fourth quarter only kind of items that we've got that don't really – are not indicative of anything going forward and some of that benefit, again we picked up in the first half of the year, which we had called out some of the benefit we picked up in the third quarter, so we don't think there's anything structurally wrong with the gross margin rates for the fourth quarter, it's just all has to do with timing.

Steven Forbes
Analyst, Guggenheim Securities LLC
Q

And then just a quick follow-up on private brand penetration, can you help us with where that rate, the penetration rate is running year-to-date? And then just remind us how private brand and brand penetration differs by quarter if it does?

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

Yeah, well. So we're not getting that into that level of granularity by quarter, but our penetration continues to increase. We're happy with our private brands, but for competitive reasons, to get too much – more granular than that, we're not going to go into it

Steven Forbes
Analyst, Guggenheim Securities LLC
Q

Okay. Thank you.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.
A

Great. Thanks.

Operator: This concludes our question-and-answer session. I would like to turn the conference back over to Ed Stack for closing remarks.

Edward W. Stack
Chairman & Chief Executive Officer, Dick's Sporting Goods, Inc.

I'd like to thank everyone for joining us on the call today and look forward to talking to you about our fourth quarter results. Thank you.

Operator: The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.