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Dick's Sporting Goods, Inc. (DKS)

Q2 2016 Earnings Call

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MANAGEMENT DISCUSSION SECTION

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

I would now like to turn the conference over to Nate Gilch, Director of Investor Relations. Please go ahead.

Nathaniel A. Gilch

Director-Investor Relations

Thank you. Good morning, and thank you for joining us to discuss our second quarter 2016 financial results. On today's call will be Ed Stack, our Chairman and Chief Executive Officer; André Hawaux, our Chief Operating Officer and Interim Chief Financial Officer; and Joe Oliver, our Chief Accounting Officer. 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.

During this call, we will be making forward-looking statements, which are predictions, projections, or other statements about future events. These statements are based on current expectations and assumptions that are subject to risks and uncertainties. Actual results could materially differ because of factors discussed in today's earnings press release, in the comments made during this conference call, and the Risk Factors section of our Form 10-K, Form 10-Q, and other reports and filings with the Securities and Exchange Commission. We do not undertake any duty to update any forward-looking statement.

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 the related reconciliations can be found on the Investor Relations portion of our website at dicks.com.

I will now turn the call over to Ed.

Edward W. Stack

Chairman & Chief Executive Officer

Thank you, Nate. Good morning. The second quarter of 2016, we're pleased to deliver results well above our previous expectations. Our diluted EPS of $0.82 per share and consolidated comp store sales growth of 2.8%, both, are well above the high end of our guidance range. Our eCommerce sales increased 26% and grew to 8.5% of net sales compared to 7.3% in the same quarter last year.

Our stronger-than-expected performance was driven by two factors. First, our guidance assumed substantial headwinds from the TSA and Sport Chalet liquidations, which we expected to continue into the third quarter. As many of you know, these were completed sooner than anticipated. We actually saw some benefit from the end of the quarter. Second, our license business benefited from the Pittsburgh Penguins and Cleveland Cavalier championships. We saw growth across most of our categories, most notably the Outdoor business. Golf comps were negative. However, we are pleased to see margin expansion for the fifth consecutive quarter.

Now, let me provide a few updates on how we remain focused on driving store productivity and overall growth throughout – through impactful merchandising and marketing strategies. On the merchandising front, Footwear is a key area of investment. At the end of the second quarter, we had 117 premium full service Footwear decks in place, and we continue to be pleased with the early sales results. We are supporting these new decks with heightened marketing efforts and an enhanced level of service and are very excited about the new brands and styles we have in place for the important back-to-school season. In addition to what we're doing in store, we're elevating our Footwear business online through improved content and a broader assortment.

To further differentiate ourselves, we continue to focus on our private brands. We remained particularly enthusiastic about CALIA, which is now our number three women's athletic apparel brand. With great brands like CALIA, Field & Stream, Quest, adidas baseball, Umbro Soccer, Top-Flite and MAXFLI, we see a lot of opportunity ahead and are targeting $1 billion in annual sales over the next few years.

Turning to our marketing, I couldn't be happier with the work our team has been doing with the United States Olympic Committee and Team USA. The Olympics have provided us a platform to deliver our highly inspirational brand message to a much broader audience than we ever have before. We've had over 200 Olympic contenders working in our stores, leading up to Rio with the mission of providing these athletes fully flexible jobs, so they can train and travel and compete. 31 of these remarkable men and women qualified for Team USA, and they all have made us incredibly proud of their accomplishments.

Also, during the quarter, we purchased TSAs intellectual property and the right to acquire 31 store leases. We were very pleased with the results of the auction, acquiring the assets that will be most impactful to our business. The customer information will be integral to our efforts to capture this displaced market share, while the rights to these stores allow us to access key markets that represent significant whitespace for DICK's Sporting Goods. Our store growth will continue to be focused on new and underpenetrated markets, where we will minimize cannibalization to our existing stores. A good example is Houston, the fourth largest city in the country, where we will be opening our first stores later this quarter.

Looking ahead, while we did start to see some benefit towards the end of the second quarter, there is still some uncertainty about how much business may have been pulled forward during these liquidations, particularly in some of the important back-to-school categories such as footwear and apparel. We believe we are poised to pick up long-term market share but remain a bit conservative until we get more distance from the liquidation events, which removed approximately $400 million of inventory from the market in a very short period of time.

As you learned from our announcement on August 12, Teri List-Stoll is no longer our Chief Financial Officer. This timing made sense, given where we were with the quarter end and the upcoming budget season. We wish Teri all the best going forward. André Hawaux, our present Chief Operating Officer and former Chief Financial Officer will assume the role of interim CFO until we announce a replacement.

In summary, we're very pleased with our second quarter results, particularly in light of the liquidation activity within the marketplace. We are focused on capturing this displaced market share and remain confident in our ability to realize meaningful share gains over the long term.

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

Andrè J. Hawaux

Chief Operating Officer & Executive Vice President, Interim Chief Financial Officer

Thank you, Ed. During the second quarter, we continued to execute on our growth drivers and expand our powerful omni-channel platform, beginning with eCommerce, where we remain on track to relaunch dicks.com on our own web platform in January of 2017.

Turning to our new stores, in the second quarter, we opened five new DICK's Sporting Goods stores, with three of them in new markets. We relocated two DICK's Sporting Goods stores to more attractive retail nodes. We also closed three DICK's Sporting Goods stores and one Golf Galaxy store.

During the third quarter, we expect to complete the bulk of our 2016 store development program, opening approximately 25 new DICK's stores and relocating four DICK's stores. We will also open approximately seven new Field & Stream stores and two new Golf Galaxy stores. 15 of our third quarter DICK's openings will be in new markets, including six DICK's stores in Houston. In total, for 2016, we expect to open approximately 36 new DICK's stores and relocate approximately nine DICK's stores. We also expect to open approximately two new Golf Galaxy stores and nine new Field & Stream stores, with all but one in the combo store format.

During the quarter, we purchased TSA's intellectual property and the right to acquire 31 store leases. The intellectual property includes the name The Sports Authority, as well as TSA's domain names, private brands, and importantly, their customer information. The leases are primarily located in new and underpenetrated markets, including California and South Florida. The lease deal was structured with maximum flexibility, where we have the right to retain or reject any or all of these leases. Our plan is to convert any TSA location we retain into a DICK's store and expect to re-open these stores over the next 12 months.

Additionally, during the quarter, we announced our plans to open a new 650,000 square-foot distribution center in Binghamton, New York. This new facility will allow us to better leverage our distribution infrastructure and support our future growth.

Lastly, one of the ways we are driving store productivity is through our new premium full-service footwear decks. And the early sales results continue to be encouraging. At the end of the second quarter, we had 117 new premium full-service footwear decks, and we remain on track to open approximately 70 additional decks in time for holiday.

I'll now turn the call over to Joe Oliver to review our financial performance in greater detail.

Joseph R. Oliver
Chief Accounting Officer & SVP

Thank you, André. Good morning, everyone. Beginning with our second quarter financial results, consolidated sales increased 7.9% to approximately $2 billion. Consolidated same-store sales, which includes all banners, both online and in-store, increased 2.8%, which was above the high end of our guidance. Within this, DICK's Sporting Goods omni-channel same-store sales increased 3%, driven by a 1.3% increase in ticket and a 1.7% increase in traffic. Golf Galaxy omni-channel same-store sales decreased 4.3%. We continued to see strong growth in our eCommerce business, which increased 26%. Gross profit for the second quarter was $597 million, or 30.36% of sales within 1 basis point of last year.

Within the gross profit section, our merchandise margins expanded, and we leveraged our occupancy expenses, but this was offset by shipping costs associated with our eCommerce business. SG&A expenses were $442 million for the quarter or 22.45% of sales, an increase of 73 basis points from the same period last year.

The deleverage was primarily driven by two items. First, we invested in store payroll as we continued to enhance the shopping experience within our stores, and to support key initiatives such as our new full-service footwear decks. Second, we also increased our administrative head count to support our growth initiatives, such as the continuing development of our eCommerce platform.

In total, led by our strong comp sales performance, we delivered earnings per diluted share of $0.82, which exceeded our high end of our guidance of $0.62 to $0.72.

Now, looking to our balance sheet, we ended the second quarter with approximately $112 million of cash and cash equivalents, and $152 million in borrowings outstanding on our $1 billion revolving credit facility. The borrowings are a result of returning capital to our shareholders and continued investments in our growth. Total inventory increased 6.2%, which is below our 7.9% sales growth for the quarter. We're very comfortable with our inventory levels and the quality of our merchandise as we transition into the fall selling season. As a reminder, our inventory still includes the winter packaways that we discussed with you as we exited 2015.

Turning to our second quarter capital allocation, net capital expenditures were $68 million, or $120 million on a gross basis. Additionally, during the quarter, we paid $16.9 million in dividends and repurchased $57 million of stock at an average price of $42.60 a share. Our year-to-date share repurchases total $107 million and we have approximately $1.1 billion remaining in our authorizations.

Now, let me wrap up with the outlook for the remainder of the year. Starting with the third quarter, as Ed had indicated, there's still some near-term uncertainty associated with the recent liquidation events, particularly in certain key back-to-school categories. Our investments and the partnership with the United States Olympic Committee and Team USA are most heavily weighted in the third quarter and we're continuing our investments in eCommerce platform during the quarter.

Taking all this into consideration, for the third quarter, we anticipate earnings per diluted share of between $0.39 and $0.42 with an increase in consolidated same-store sales of between 2% and 3%. Third quarter operating margin is expected to decline compared to the same period last year due to higher SG&A expenses for the initiatives that we just discussed, partially offset by an increase in gross margin.

Looking at the full year, we're raising our guidance and now expect earnings per diluted share of between $2.90 and $3.05. This compares to our prior guidance of between $2.60 to $2.90. We now expect consolidated same-store sales to increase between 2% and 3%.

To remind everyone, our earnings this year are impacted by approximately $50 million to $55 million, as we're investing in three key initiatives. First is the transition and growth of our eCommerce business. Second is our brand building through our sponsorship with the United States Olympic Committee, and third is a rollout of our full-service footwear decks.

As a result, the higher SG&A expenses, with some partial relief from gross profit improvement, will cause operating margins to decline year-over-year. Net capital expenditures for the full year of 2016 are now expected to be approximately $275 million, or about $450 million on a gross basis. The increase versus our prior expectation is primarily driven by our new distribution center.

Please note that our earnings per diluted share estimates do not include certain costs to integrate The Sports Authority stores into our operations. These costs include occupancy expenses incurred while converting TSA stores to the DICK's brand, costs incurred to ready these stores for the grand openings, and other professional fees related to the transition. We will separately report these costs to you beginning with our third quarter results.

I will now turn the call back over to Ed for some final comments.

Edward W. Stack
Chairman & Chief Executive Officer

Thanks, Joe. It's clear that DICK's Sporting Goods has significant growth opportunities ahead with the acquisition of TSA's intellectual property to the meaningful growth in our digital business to the investments our key partners such as Nike, Under Armour, and The North Face continue to make with us, to enhance the consumer experience both in-store and online.

DICK's is poised to capture a significant amount of the displaced market share out there today. I believe this is evident in our second quarter results. Last but not least, I would like to thank our over 30,000 associates for their hard work and thoughtful strategies. They are the team that has made DICK's Sporting Goods successful.

Operator, this concludes our prepared remarks. We would like to open it up for questions. Thank you.

QUESTION AND ANSWER SECTION

Operator: We will now begin the question-and-answer session. [Operator Instructions] At this time we will pause momentarily to assemble our roster. Our first question comes from Robby Ohmes of Bank of America. Please go ahead.

Robert F. Ohmes
Bank of America / Merrill Lynch

Q

Good morning, Ed. How are you?

Edward W. Stack
Chairman & Chief Executive Officer

A

Hi, Robby. How are you?

Robert F. Ohmes
Bank of America / Merrill Lynch

Q

I'm good. Listen, I was hoping you could maybe give us a little more color on the cadence through this quarter in terms of trends in stores that were overlapping with The Sports Authority, maybe a little more color on how much full-service footwear shops – were they meaningful in helping on this quarter? And maybe remind us how – do you usually see – are you seeing a lift from the Olympics? Did you see that in July, or is that something that's really helping you in August? Thanks.

Edward W. Stack
Chairman & Chief Executive Officer

A

Sure. Well, Robby, the – it is the stores closed up – so we're not going to get into a lot of detail, but the stores that were competing with The Sports Authority are outperforming the balance of the chain. So, we're definitely seeing market share coming to us from the closings. The full-serve footwear we – these things have kind of rolled on, on a weekly basis, so we didn't see much of an impact yet. Although, the sales results that we've seen of the stores that have been open for a while are very positive. We expect to see more of an impact in the third quarter of these full-service footwear decks than we saw in the second quarter. Although, we do remain a bit cautious on footwear as The Sport – we're not sure how much The Sports Authority and the Sports Chalet liquidations are going to have on that. Sports Authority, from what we understand, liquidated a little less than a million pairs of cleats and over 2 million pairs of athletic footwear. And so, we don't know what that's going to do to the third quarter.

As far as the Olympics go, we haven't seen a big impact on Olympic merchandise, although as we talked about in the call, we've been very aggressive with our marketing with the Olympics. Our team has done a great job on how we've partnered with the U.S. Olympic Committee and Team USA, and we think we got our message out, and have had very positive comments back on our marketing message around the Olympics. And then, the other aspect that helped our business were the playoffs in hockey and the NBA. So, to have the Pens win the Stanley Cup was certainly helpful to our business and to have the Cavs win the NBA championship was helpful to our business, and Cleveland responded great to the championship merchandise.

Robert F. Ohmes
Bank of America / Merrill Lynch

Q

Got it, that's really helpful. Thanks, Ed.

Edward W. Stack
Chairman & Chief Executive Officer

A

Thanks, Robby.

Operator: Our next question comes from Seth Sigman of Credit Suisse. Please go ahead.

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

Q

Thanks. Good morning, and nice quarter, guys. Ed, you discussed the benefits late in the quarter from some of those competitor closings, but then, a couple of comments about the uncertainty regarding the pull forward here in the third quarter, which makes sense. I'm just wondering, is that based on what you're seeing right now or are you just taking a conservative view of the different scenarios?

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, it's not necessarily what we're seeing right now, but the merchandise in the second quarter is a little bit different than the third quarter, so that, that outdoor category, and I'm not talking about the hunt fish piece but the outdoor camp piece; canopies, chairs, outdoor camping merchandise is very important to us in the second quarter as Sports Authority was liquidating. We think people came to us for those type of products. As we said, our outdoor category was very good in the second quarter. We're concerned that there may be this liquidation of $400 million worth of merchandise, a big part which is athletic footwear and apparel could impact us on the third quarter. People may have done some early back-to-school shopping with the liquidations that they have. So we just don't know, and we won't know for – we won't know for a couple of weeks.

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

Q

Okay. That make sense, and then just a follow-up question on store growth, maybe two parts here. First, just regarding the store rights that you've acquired, as you look to next year, is there a view here where maybe you could accelerate your store openings or is the plan to basically just cherry pick and use any of those acquired stores as a – or in lieu of any of the previously planned stores? And then, the second piece of it is as you think about a market without one of your large competitors, does it change your view on the ultimate store target or how to think about the pace of store growth and if you need to continue at this current pace? Thanks.

Edward W. Stack
Chairman & Chief Executive Officer

A

So as far as accelerating the store growth, we've got 30 stores – we've got designation rights on 31 stores. We don't expect that we're going to open up all 31 stores. We've already – there is a few that we know that we're not going to open up because we couldn't make the right deal and we've walked away from them. But I'm not going to give me a lot of detail on that right now as we're still kind of working through this, but it won't be 31 stores that we open up. Our store growth next year will probably be a little bit higher than it was this year because of the TSA stores, but we expect our growth to remain kind of in the same zone that has been. With these liquidations, we think that there's not a need to accelerate the store growth.

Our total store count probably hasn't changed an awful lot, although we'll probably go, as we said, the same pace, and our big focus is to drive our digital business, which you can see that we're doing this, that we've made these big investments. This business continues to accelerate and we think we're poised to really drive this business going forward.

Andrè J. Hawaux
Chief Operating Officer & Executive Vice President, Interim Chief Financial Officer

A

And, Seth, this is André. I would add two things. One is many of the stores that we're looking at are in markets that we currently do not serve and they're underpenetrated, so we believe this would be a nice complement to the fleet we already have. And the other thing investors need to know is we're going through the same rigor with these leases as we do with our real estate strategy. So we're going through the same analysis we would do on a brand-new DICK's store to make sure that it pencils and that it makes economic sense for us to open, otherwise, we have flexibility not to take a lease.

Edward W. Stack
Chairman & Chief Executive Officer

A

And of these 31 stores, we have the designation rights to, the vast majority – 20 stores of the 31 stores are in California and Florida where we are very underpenetrated.

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

Q

Okay, thanks. Very helpful.

Edward W. Stack
Chairman & Chief Executive Officer

A

Sure.

Operator: Our next question comes from Michael Lasser of UBS. Please go ahead.

Michael Louis Lasser
UBS Securities LLC

Q

Good morning. Thanks a lot for taking my question. Ed, how long do you think that this benefit from the market consolidation is going to last? Is it the type of thing where you're going to see some share gains for the next four quarters and then that will normalize? Or should we expect that the tailwind is going to last longer than that?

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, again, we're not 100% sure, but I think it – I would think the tailwind is going to last longer than that with these. Because not only the fact that these competitors are gone, the fact that they will no longer be opening stores and intruding in some of our markets, we think it will be positive also. So, there's kind of a double-edged benefit, if you will, that they left some markets, and then they're not going to be opening up in markets that intrude on our market share. So, we think this is going to last for a while.

Michael Louis Lasser
UBS Securities LLC

Q

And then philosophically, how do you think about the margin windfall that you should experience from abnormally high comps for the next several quarters, at least? Do you allow that to fall to your bottom line and reward some of the shareholders, or do you reinvest that back into the business and put it off for a rainy day?

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, I think it'll depend on a couple of things. And I suspect some of it will go to – go back into the business, which we think – no matter what we do, we think it will reward the shareholders longer term, whether it's having something drop to the bottom line right now or continue to invest in the future of our business, which will certainly benefit us going forward. So, we'll take a look at this, and there will be some that will come to the bottom line and some that will go to – continuing to make investments in our business.

Michael Louis Lasser
UBS Securities LLC

Q

And my last question is just on your relationship with your vendor community, and how that's unfolding now that the market is consolidating. Do you feel like the tenor of your conversations and the nature of your relationship, especially with your key vendor partners, is changing, where you're becoming that much more important?

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, it's always been good with our key partners, such as Nike, Under Armour, The North Face, those brands. It's always been very good. And it continues to get better, as you continue to see them investing in our stores. We'll have a new roll-out of Nike shops in the Houston stores when we open them. We continue to have investments from the North Face, Under Armour. So, it's – they've always been good, they continue to be good. And we really work this partnership. We're not trying to get one up on them. I don't think they're trying to get one up on us. We really go to the market as true partners.

Michael Louis Lasser
UBS Securities LLC

Q

Okay. Thanks so much.

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

Camilo Lyon
Canaccord Genuity, Inc.

Q

Thanks. Good morning, Ed, and everyone else. How are you?

Edward W. Stack
Chairman & Chief Executive Officer

A

Hi.

Camilo Lyon
Canaccord Genuity, Inc.

Q

Ed, I was hoping to get a little bit more detail on how you view your promotional stance. I think in years past, you've talked about competitors in the marketplace becoming more promotional and you meeting that promotional cadence, so that you would not suffer some traffic losses to that. With TSA now gone, how do you view now that promotional stance, as – and particularly as we head into the back-to-school and holiday season?

Edward W. Stack
Chairman & Chief Executive Officer

A

We think it will probably – we expect it, although, you never know what somebody else is going to do. We expect the promotional environment to be no worse than it's been in the past, and we think a little bit better.

Camilo Lyon
Canaccord Genuity, Inc.

Q

Okay. Great. And then with respect to the IP that you won at auction, have you begun to use that data? Have you seen any benefits from that data? And if the customer's coming over to the DICK's platform? And if you haven't begun using it, when will you, and how will that inform your targeted kind of roll-out of stores and really a messaging that you wanted to convey to those customers?

Edward W. Stack
Chairman & Chief Executive Officer

A

Yeah. So, we're seeing some benefit right now, based on – if the stores being closed, but we haven't really – we just closed on this not long ago. We're just getting this information, starting to sort through it. We think – we hope that it will be helpful to us in the fourth quarter, a little bit in the third quarter, but more so in the fourth quarter.

Camilo Lyon
Canaccord Genuity, Inc.

Q

Okay. And then just the last one, Ed. You touched upon a little bit, with respect to the Q3 guidance, with regards to how much inventory has been taken out of the market already, given the liquidations. Is there anything else that would help explain why you would anticipate a deceleration on a two-year basis in the Q3 comps now that the stores have completely shuttered, the TSA stores?

Edward W. Stack
Chairman & Chief Executive Officer

A

No. We're just – the only thing it is, is just how much was taken out of the marketplace, and especially for the back-to-school season, because Footwear, as a percent to our business and Apparel – Athletic Apparel, as a percent to our business is a very big part of our business in the third quarter. And they took out – like I said, they took out almost 1 million – liquidated 1 million pair of cleats, so soccer cleats, football cleats, baseball cleats, and then an awful lot, even more so than that, athletic footwear in the marketplace that some people probably did some – we think did some early back-to-school shopping during these liquidations. So, we just don't know how this is going to play out. But we think, long term it's great for us. I mean, I don't think it'll have any impact – it'll have no impact on us in the fourth quarter, we don't think.

Camilo Lyon
Canaccord Genuity, Inc. Q

Was there any category that TSA was particularly stronger at than you that you think would be an opportunity for you to rapidly accelerate your share in that particular category, whether it's outerwear or some other category that you might not have had as big a mix representation in your own business?

Edward W. Stack
Chairman & Chief Executive Officer A

From what we've seen – well, one, we always knew. The other one we kind of seen at the store. We didn't think it was doing as well as it probably was. But they were always a better tennis store than we are. So, I think, there's some opportunity in tennis. But that's a very small business and not going to move the needle. What we've learned is that they did a better – a bigger fitness business than we had anticipated. And we think around fitness, whether it's cardio, other fitness products, we think we've got an opportunity in fitness to grab significant market share.

Camilo Lyon
Canaccord Genuity, Inc. Q

Got it. All the best to you in the upcoming back-to-school and holiday season.

Edward W. Stack
Chairman & Chief Executive Officer A

Great. Thanks.

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

Simeon Ari Gutman
Morgan Stanley & Co. LLC Q

Thanks. Good morning. Nice quarter, Ed.

Edward W. Stack
Chairman & Chief Executive Officer A

Thanks.

Simeon Ari Gutman
Morgan Stanley & Co. LLC Q

Different topic for a minute, on Eagle investments, as we head into next year, can you just talk about any – and just give us a sense of how it's going, any changes to the investment cadence? Anything that, I guess, popped up one way or the other, good or bad, as we roll into next year and you take on independence with regard to the online platform?

Edward W. Stack
Chairman & Chief Executive Officer

A

Yeah, no. We're very pleased with where we are. Some of the things that we needed to get done have been done. We've actually in the test stage taken orders and shipped product. So, we're moving in the right direction. We don't see any red lights right now. The capital that we had anticipated is coming in on budget. We're – as of right now, systems are green.

Simeon Ari Gutman
Morgan Stanley & Co. LLC

Q

And you called out, I guess, free shipping as a headwind. Was it any more of a headwind than you anticipated, or it's about what you've expected?

Edward W. Stack
Chairman & Chief Executive Officer

A

It's about what we expected. It's just different than last year. It's going to continue – as this business continues to increase, it's going to become a larger part of our expense structure, or margin rate structure.

Simeon Ari Gutman
Morgan Stanley & Co. LLC

Q

Got it. Okay. And then my follow up. I guess, this is sort of implicit, given that there seems to be some conservatism in the third quarter, but I was going ask you, if you back into the fourth quarter, I think it looks like it's somewhere between a 3% to a 4%, if the math is right there. And yet your Q4 compare is very easy, much easier than what you just did this quarter. And so, it looks like there's conservatism as the rest of the year goes on. But I just want to confirm that, and if there's any reason why by the fourth, if you're doing 2% to 3% now, why you can't do even better than what's implied by the time we get to the end of the year?

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, it's still an uncertain environment out there with what some other retailers might do. It's an uncertain environment out there with the presidential election. It's uncertain out there from a weather standpoint. So, I agree with everything you said, but there's still some uncertainty out there.

Simeon Ari Gutman
Morgan Stanley & Co. LLC

Q

Okay. Thanks. Good luck.

Edward W. Stack
Chairman & Chief Executive Officer

A

Thanks.

Operator: Our next question comes from Matthew McClintock of Barclays. Please go ahead.

Marjorie Lopez Marinez
Barclays Capital, Inc.

Q

Hi. This is Marjorie Lopez on for Matthew McClintock. Thank you for taking our question. My first question is can you elaborate on your Golf business? How do you believe you're positioned in this business, particularly given that one of your partners decided to exit the Golf equipment? Thank you.

Edward W. Stack
Chairman & Chief Executive Officer

A

Sure. Well, I think in the – as far as the Golf business goes, I think, we're very well positioned. But it's been a difficult – it's kind of a bit more of a difficult business from a sales standpoint. But don't lose the fact, and we've talked about this, that the margins have increased. So, a lot of the products that had been in the marketplace that needed to be liquidated, those are out of the market today. And although sales are down a bit, the margin rates are up. And this is the fifth consecutive quarter that margin rates are up.

There is some consolidation going on in the wholesale side of the business. I think there'll be some consolidation on the retail side of the business. But as far as in the Golf business, I think we are very well-positioned. And our Golf business – we remain committed to our Golf business. And understand, our Golf business is profitable. It's not a drag on earnings. Our Golf business is profitable.

Marjorie Lopez Marinez
Barclays Capital, Inc.

Q

Great. Thank you.

Edward W. Stack
Chairman & Chief Executive Officer

A

Yes.

Marjorie Lopez Marinez
Barclays Capital, Inc.

Q

And just a quick follow up. I know that another area for growth is product development. How has CALIA performed? And are you making other improvements across your other private brands? And also, if there are any other categories where you see an opportunity for private label? Thank you.

Edward W. Stack
Chairman & Chief Executive Officer

A

Sure. Yeah, our PD – our product development business we're very enthusiastic with and CALIA has done great. For CALIA to move to be the number three women's athletic brand in a year and a half since we launched it – a year and 16 months since we launched it, is great. So we continue to invest in that brand. You'll see us investing heavier next year in that brand. And as we take a look at what we're going to do from a PD standpoint, we're continuing to be enthusiastic about Field & Stream, we continue to be enthusiastic about Quest and some other outdoor categories. And we're pretty confident we can move this private brand business to exceed $1 billion over the next couple of years.

Marjorie Lopez Marinez
Barclays Capital, Inc.

Q

Great. Thank you.

Edward W. Stack
Chairman & Chief Executive Officer

A

Thank you.

Operator: Our next question comes from Stephen Tanal of Goldman Sachs. Please go ahead.

Stephen Tanal
Goldman Sachs & Co.

Q

Good morning. Thanks, guys, for taking the question.

Edward W. Stack
Chairman & Chief Executive Officer

A

Sure.

Stephen Tanal
Goldman Sachs & Co.

Q

Just wanted to, I guess, figure out sort of the inflection from TSA and understand how that might have moved. And I guess maybe really just asking Simeon's question in a different way, can you maybe size the Penguins' and the Cavs' championships in the quarter as we sort of think about what the 2Q kind of trend rate to 3Q implied guide might look like as we think about TSA kind of rolling in?

Edward W. Stack
Chairman & Chief Executive Officer

A

So, could we? Yes. Are we? Probably not from a competitive reason. We're not going to tell you much business we did with those two. But I will tell you that the Pens and the Cavs were meaningful to the quarter and certainly very helpful to the quarter. The Cavs, more so than the Pens. The TSA, the stores where TSA closed, where we're closing did better than the balance of the chain. So, kind of how that thing – how that laid out, we're not going to get that granular from a competitive standpoint, but TSA, Cavs, Pens were all very helpful to the quarter.

Stephen Tanal
Goldman Sachs & Co.

Q

All right. Fair enough. And you mentioned strength in the Outdoor category, but not firearms and ammo. Could you talk about sort of the subcategories and whether you saw any movement on the gun side?

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, that business has been kind of up and down and depends on what's happening in the news, unfortunately, and on the political climate. But the majority of our Outdoor business is driven by that outdoor category, which is camp, water sports, paddle sports. And that business has really been very good. Our team has done a wonderful job focusing on that, on those businesses. And as you take a look at – and, I mean, the gun business was positive, but we have no idea – the gun business is somewhat volatile, but in the second quarter it was positive.

Stephen Tanal
Goldman Sachs & Co.

Q

Understood. And just last one for me. There is a recent announcement at the department store front. I guess, another one of these companies getting more athletic apparel. How do you guys think about that? And any comments you might make on that front would be appreciated. Thanks.

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, the way we're looking at this is that The Sports Authority is out, somebody else is going to carry an important brand. We think it's probably net neutral. It might be slightly net negative based on the number of stores they have, but we don't think it's really meaningful. And we have a differentiated assortment there. So I think it's – I mean, we wish it wasn't happening, but we don't think it's really a big impact.

Stephen Tanal
Goldman Sachs & Co.

Q

Got it. Thanks so much.

Edward W. Stack
Chairman & Chief Executive Officer

A

Sure.

Operator: Our next question comes from Sam Poser of Susquehanna. Please go ahead.

Samuel Marc Poser
Susquehanna International Group, LLP

Q

Good morning. Thank you for taking my questions.

Edward W. Stack
Chairman & Chief Executive Officer

A

Sure.

Samuel Marc Poser
Susquehanna International Group, LLP

Q

First of all, on the merchandise – can you give us the specifics on the merch margin and the fixed cost, just the improvement and the leverage or deleverage?

Joseph R. Oliver
Chief Accounting Officer & SVP

A

Yeah, Sam, this is Joe. So, we're not going to talk about the specific number, but I would say between merch margin and the occupancy leverage, the basis point improvement was about the same, and then offset with the increased shipping costs.

Samuel Marc Poser
Susquehanna International Group, LLP

Q

Okay. Thank you. And then when you think about – I mean, between TSA and Sport Chalet, they did probably $3.2-ish billion annually. When you think about that over time, I mean, how much of that business do you think you can get? Just sort of on where we are today, forget about the store openings and all that other stuff. Just from a share basis?

Edward W. Stack
Chairman & Chief Executive Officer

A

No, we're not going to go out, and I think you probably wouldn't either if you were sitting on this side of the table, Sam. We're not going to go out and throw a number out there, but I can tell you, we are going to aggressively go after as much of this share as possible. We've gone down to the very granular level of where we think – categories that we think we have a big opportunity to grab market share. We think we have a meaningful opportunity to grab share in the Footwear business and the Apparel business. We think that we've got an even bigger opportunity to grab a bigger part of the market share on the team sports area: baseball, football, soccer, and those.

We think we've got an opportunity to take a bigger market share in the fitness business. And we think in Sports Authority's Outdoor category, which was really more backyard-type camping, we think we've got a big opportunity to do that. And we think we saw pretty good results in the second quarter in that Outdoor category coming from TSA. So, we've got this pretty granular. Our teams are monitoring these stores very closely, making sure that we funnel merchandise into these stores as fast as we can. I will tell you, we've gotten surprised in some areas of the country that it's growing at a faster pace than we had anticipated, and – such as South Florida.

Samuel Marc Poser
Susquehanna International Group, LLP

Q

Gotcha. And then lastly, I mean, speaking of South Florida, you've got the rights to the 31 stores. You're going to – it sounds like you're going to give a few back. But are there other stores where you wanted them, but it just didn't work, and you're going to go back to the landlords and say, – and have further discussions? So, that number could go up in total, just working a different kind of deal? I mean, I won't – I don't – I couldn't imagine there's a ton of them, but are there more there, or is that 31 stores in total sort of what you wanted?

Edward W. Stack
Chairman & Chief Executive Officer

A

Those 31 stores, Sam, are the 31 stores that we wanted. I will tell you, there was one other one we – there was actually two other ones we did want that we didn't get, and somebody else got them, so that's off the table, no problem. But there's nothing else sitting out there that we're trying to negotiate with the landlord to get. We got everything that we wanted, except two.

Samuel Marc Poser
Susquehanna International Group, LLP

Q

And lastly, in the one in Florida, Sunrise, that's Sawgrass Mills, I assume?

Andrè J. Hawaux
Chief Operating Officer & Executive Vice President, Interim Chief Financial Officer

A

That's correct.

Samuel Marc Poser
Susquehanna International Group, LLP

Q

Okay. Well, thank you very much. Good luck.

Edward W. Stack
Chairman & Chief Executive Officer
A

All right. Thanks.

Operator: Our next question comes from Kate McShane of Citi Research. Please go ahead.

Kate McShane
Citigroup Global Markets, Inc. (Broker)
Q

Hi. Thanks. Good morning.

Edward W. Stack
Chairman & Chief Executive Officer
A

Hi, Kate.

Kate McShane
Citigroup Global Markets, Inc. (Broker)
Q

My first question was just with regards, again, on the new stores, especially in California and South Florida. Are you taking the time to just gather some learnings in that market before you convert to the TSA stores – before you convert the TSA stores there? And any insights into what you may have to do differently in those markets versus the rest of your fleet?

Andrè J. Hawaux
Chief Operating Officer & Executive Vice President, Interim Chief Financial Officer
A

I'll start with – and Ed can add to this. But I think we are, as I mentioned, first, on the economics and the way we think about the real estate transaction, we're being very consistent with how we look at the financials for whether the lease makes sense for us to get there. As Ed also mentioned, the merchants are doing a very deep dive, understanding market by market, where they excelled or where that customer was really going.

So, in some markets, that'll see us accentuate categories, such as fitness. In some markets, there may be some tennis accentuation that we see, but also, clearly, Footwear and Athletic Apparel, where we were strong and they were pretty good as well. In Southern California and South Florida, you'll see swim play a different role in our stores there. So, very much, the merchants and the allocators are taking a very granular view of those markets to determine how we assort those stores to meet the customers' expectations. I don't know if you want to add anything, Ed?

Edward W. Stack
Chairman & Chief Executive Officer
A

One of the other things we've done, Kate, is we've talked to the brands to say, okay, based on this market share that's being displaced, what was – in order for you to continue your business and market share, what advice do you have for us in some of these stores in California and Florida and a couple of other places? And the brands have been very helpful working with us on these learnings also. Understand also that the majority of these stores, we've got stores in the general vicinity. We may not be in that particular trade area, and we need to go into that trade area, but we've got a number of stores in Florida, we've got a number of stores in California, and we've got a sense of what needs to be done there.

Kate McShane
Citigroup Global Markets, Inc. (Broker)
Q

Okay. Great. And I think, Ed, you'd mentioned maybe last quarter that there were opportunities to buy some inventory at a discount. Did that contribute much during the quarter? And do you continue to benefit that for the next couple of quarters going forward?

Edward W. Stack
Chairman & Chief Executive Officer
A

I don't think it's the next couple of quarters. We've got – we did have the opportunity to buy some product off-price. Some of the product that we bought off-price, we actually have bought and packed away for promotions going into next year, beginning the year, new store openings, so it's helpful. We did buy some product off-price. I don't think – with the size of our business and what we bought, I don't think you'll – if we didn't tell you we did that, you probably wouldn't – you wouldn't even know. It won't have a huge – it won't drive the needle a whole lot.

Kate McShane
Citigroup Global Markets, Inc. (Broker)
Q

Okay. Thank you.

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

Michael Baker
Deutsche Bank Securities, Inc.
Q

Thanks. A couple of sort of follow-up questions. One, I just want to understand this. So, the stores that were against The Sports Authority, they did better than the chain. But I assume, does that include some negative impact early in the quarter when The Sports Authority stores were in liquidation? And then as liquidations ended, the DICK's stores saw a bump in the net result through the quarter was a positive? Is that the right way to think about it, or even when The Sports Authority stores were liquidating, the DICK's stores were out-comping?

Edward W. Stack
Chairman & Chief Executive Officer
A

It's a little of both, but more the former than the latter. So, there was some pressure to begin with. And as the liquidation – as there were less good products there, we started to see some market share. As you can imagine, over the first several weeks, all the good stuff got cherry picked pretty good, and they got left with the dregs. So, it was helpful as we got closer to the end of the liquidation.

Michael Baker
Deutsche Bank Securities, Inc.
Q

So, in that sense, can we infer that the comp trends got better throughout the quarter?

Edward W. Stack
Chairman & Chief Executive Officer
A

Well, it's kind of – it's a little bit difficult, because we did have – the Cavs and the Pens were an important part of that comp trend also, which was earlier in the quarter.

Michael Baker
Deutsche Bank Securities, Inc.
Q

Okay. Understood. Two other unrelated – well, I guess, somewhat related follow-ups. One, how do you think about your sort of fixed costs or variable cost – when you see a sales windfall from these types of things, do you need to add a lot of store labor or marketing around it? Or – just we can sort of gauge the flow-through of the incremental sales.

Edward W. Stack
Chairman & Chief Executive Officer
A

Nothing really significant. So, will we add some store payroll? Sure. So, as the store gets busier, we'll add some store payroll in the form of associates on the floor or cashiers to try to check people out quickly. Marketing – not an awful lot from a marketing standpoint that we need to add to these trade areas where TSA went out. So there's a relatively good flow-through.

Michael Baker
Deutsche Bank Securities, Inc.
Q

Okay. Yeah, that's encouraging. Lastly, the comment about shipping costs impacting the gross margins, which is understandable. But I'm wondering, is that a function of just a big increase in eCommerce? And said differently, are you seeing an improvement in your shipping costs but it's still a bigger drag because eCommerce is bigger than it was a year ago because it's up 26%? Are you make any progress in lowering your costs, though?

Edward W. Stack
Chairman & Chief Executive Officer
A

We've worked on how to lower the costs or mitigate those increases. Our team's done a really nice job. The vast majority of this is because of the increase in penetration. Just we're doing so much more business digitally.

Michael Baker
Deutsche Bank Securities, Inc.
Q

And is that going to be less of a drag once you flip the switch on taking the eCommerce in-house in 2017?

Edward W. Stack
Chairman & Chief Executive Officer
A

It's not necessarily from a shipping standpoint, but there will be other cost drags that will not be there any longer. As we said, we'll get a roughly 25-basis point improvement in operating margin when we flip the switch.

Michael Baker
Deutsche Bank Securities, Inc.
Q

Primarily on the SG&A line I think is what you said.

Edward W. Stack
Chairman & Chief Executive Officer
A

Yes.

Michael Baker
Deutsche Bank Securities, Inc.
Q

Right. Okay, understood. Thanks for all the color.

Edward W. Stack
Chairman & Chief Executive Officer

A

Thank you.

Operator: Our next question comes from Scot Ciccarelli of RBC Capital Markets. Please go ahead.

Scot Ciccarelli
RBC Capital Markets LLC

Q

Hi, guys. Scot Ciccarelli. Would you have expected more gross margin pressure in the quarter, given the TSA liquidation process?

Edward W. Stack
Chairman & Chief Executive Officer

A

No, we really didn't. We indicated that we were – in the last call, I think we indicated that we weren't going to go chase the liquidation prices, that we were going to let them just liquidate their product and we'll get the benefit after they're done, but we weren't going to go try to chase the liquidation and take our margin rates down.

Scot Ciccarelli
RBC Capital Markets LLC

Q

Got you. And then a little bit of a different subject, and I suspect it's a little taboo, but is there any different messaging from the company, whether it's on the expense side or any other front, frankly, relative to what Teri has been telling us now that she's no longer in the CFO seat?

Edward W. Stack
Chairman & Chief Executive Officer

A

No.

Scot Ciccarelli
RBC Capital Markets LLC

Q

Okay, that's all I need. Thank you.

Edward W. Stack
Chairman & Chief Executive Officer

A

Okay. Thanks.

Operator: Our next question comes from Mitch Kummetz of B. Riley. Please go ahead.

Mitch Kummetz
B. Riley & Co. LLC

Q

Yeah, thanks for taking my questions. Ed, you talked about a little bit of uncertainty given your potential pull forward on some categories like footwear, cleats things like that. Are there any categories where there really should be no pull forward? I'm thinking about maybe some fall Team Sports, things like that or maybe TSA didn't have that inventory at the time that they were going through liquidations? And if so, is that potentially meaningful to the third quarter?

Edward W. Stack
Chairman & Chief Executive Officer **A**

Well, I mean, so are there some things like I'm not sure how they were in stock on mouth guards for football soccer, receiver gloves, all that. So, do they pull some of that forward? Probably. I don't know how significant it was, but the main thing that we are concerned about and it's so important to our third quarter business is footwear and athletic apparel. And I just think some people went and stocked up a little earlier. I mean, I know some people did. How – what the impact is we don't know yet, but we think that there is a huge, a very big opportunity for us going forward as we get further away from these liquidations.

Mitch Kummetz
B. Riley & Co. LLC **Q**

Got it. And in terms of some of the liquidations in the quarter, again, you mentioned athletic footwear 2 million pairs, to what extent did that have a negative impact on your footwear business in the quarter? Is there any way to kind of quantify that? I mean, was your footwear business potentially down in the quarter because of it? Or...

Edward W. Stack
Chairman & Chief Executive Officer **A**

No. It's tough to put that – to give that, kind of what that number would be, because we had a lot of noise in our footwear business also, that we were renovating a number of these decks. And these decks, as you can imagine, and what expect us to, we made the investments in our best stores. So as we're going through this transition, building out these decks, it put some pressure on our footwear business because it was a relatively difficult shopping experience as we were going through the modification of these footwear decks. After we did it, our footwear business in those areas have been really good and have outperformed the chain. So, there's just a little too much noise right now to come to a conclusion in the second quarter.

Mitch Kummetz
B. Riley & Co. LLC **Q**

Got it. And then last question, in terms of the 31 stores you have the rights to and how many you might be going forward with, I think you made the comment that you'd reopen those stores within the next 12 months. I guess that's further out than I would've anticipated. I would've guessed you'd make a decision kind of retrofit and most of the stores would kind of come online at the same time. First of all, is it still kind of a four to five months on a retrofit? And, I mean, at some point are you going to kind of come to a decision on the stores? How does that work? Is it all sort of individually negotiated with the landlords?

Andrè J. Hawaux
Chief Operating Officer & Executive Vice President, Interim Chief Financial Officer **A**

Well, a couple of things there, Mitch. This is André. One is there are individual discussions that are going on. We do have a timeframe and that's going to be the first week of September where we have to make some of these decisions because we want to be able to – in the event that we do reject, we do want to walk away and not have any costs as a result of the rejection. The other piece will be in the markets that we're going, where the bulk of these stores are, California and South Florida, the permitting process for us to do the stores the way we want to do them is going to take some time. So, it varies by jurisdiction. Some will be opened earlier than others, but I think there will be some long lead time items relative to permitting that is required for us to build.

As you know, California has a lengthy permitting process and parts of Florida do as well. So our goal is to get these opened as soon as possible and to make sure that we're providing that customer the experience and the shopping experience that they're used to at DICK's Sporting Goods. So we're going to do the right things for that and get them open as soon as we can.

Mitch Kummetz
B. Riley & Co. LLC

Q

Okay, appreciate the color. Thanks, and good luck.

Operator: Our next question comes from Dan Wewer of Raymond James. Please go ahead.

Dan R. Wewer
Raymond James & Associates, Inc.

Q

Thanks. Ed, I wanted to ask you about the Field & Stream combo stores. We thought originally a few years ago when you were still using the freestanding model, you are looking at potentially 50 stores by 2017. And then, I guess the following year, we dialed that target back. But given the success of the combo stores, what are you now thinking is the art of the possible for the large Field & Stream formats? And then also, if you could talk about in those stores that are located near Bass Pro or Cabela's, how they perform against those stores without those competitors.

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, the stores that don't have Bass Pro or Cabela's do a little better than the ones that do have Bass Pro or Cabela's. They're both very good competitors. As we take a look at these combo stores, we're very enthusiastic about the combo stores. We just opened up one in Albany, New York, relocated a DICK's store, just opened up one in Albany, New York, and it has done great. We've got a couple of them that are going to be opening in Houston in this next quarter. We've got several of them for next year. We think that there is – we haven't come out to say exactly where, how many we can put out there, but we still expect this to be an important part of our store development program. Where we've done these combo stores, we have been very pleased with them.

Dan R. Wewer
Raymond James & Associates, Inc.

Q

So in Houston, where you picked up some TSA leases, you're able to get some adjacent space that's large enough to support the combo format?

Edward W. Stack
Chairman & Chief Executive Officer

A

No. No. No. There's no TSA store that will be converted to a combo store. The stores in Houston are coming right up out of the ground as part of our development program in Houston. And remember, we don't have a DICK's store in Houston today. We don't have a DICK's store. We don't have a Field & Stream store in Houston today.

Dan R. Wewer
Raymond James & Associates, Inc.

Q

And second question, What are your thoughts on the status of athletic footwear and apparel? And the reason I'm asking is some of your competitors are telling me they've been disappointed with the lack of innovation in apparel relative to footwear from the key vendors in the industry.

Edward W. Stack
Chairman & Chief Executive Officer

A

We're still very pleased. We're happy with our business. We're very happy with the footwear business. We continue to be very enthusiastic about what we're doing with the CALIA brand on the women's side, and we're talking about what else we can do on the athletic side to bring in another athletic brand that would go across men's, women's, and kids that would be more of an opening price point brand. So we continue to be very enthusiastic about what's going on with apparel and footwear. When we get to Houston, you'll see a new Nike concept on the floor from an apparel standpoint that we've been working on with them that we expect will be rolled out to a number of stores going into next spring. So, we continue to be very excited about it.

Dan R. Wewer
Raymond James & Associates, Inc.

Q

Okay. And then the last question, I think, Joe, you had mentioned in your prepared comments that you would exclude the occupancy costs for the TSA stores until they opened, which makes sense, but I think you also indicated you would exclude some of the preopening expenses as well from the figures that you released going forward. I was curious as to why those would be carved out, just the preopening expense component?

Joseph R. Oliver
Chief Accounting Officer & SVP

A

Yeah, so it would just be some of the preparation costs associated with getting the store ready, so it's kind of no different than what we've done in the past when we'd picked up some of the stores from Galyan's and kind of went through that conversion process.

Dan R. Wewer
Raymond James & Associates, Inc.

Q

Is it a lot more expensive than if you were to – than the expense with a greenfield location?

Joseph R. Oliver
Chief Accounting Officer & SVP

A

They're going to be different. Yeah. So as Andrè said, we've got a long permitting process that we have to go through that'll be a bit different. And then, like I said, a lot of dead rent, those types of costs that we're going to incur. So, those will all be the items that we're going to call out going forward.

Dan R. Wewer
Raymond James & Associates, Inc.

Q

Okay, thank you.

Operator: Our next question comes from John Kernan of Cowen. Please go ahead.

John Kernan
Cowen & Co. LLC

Q

Good morning, guys. Thanks for squeezing me in, and congrats on a really strong quarter.

Edward W. Stack
Chairman & Chief Executive Officer

A

Thank you.

John Kernan
Cowen & Co. LLC

Q

Ed, I think on an earlier call you had blessed mid-teens earnings growth off of this year's base. Obviously with the $55 million in costs related to footwear, the Olympics and the transition of eComm rolling off, it seems like that could potentially be conservative given the new run rate of the business coming out of Q2. Are you thinking any differently about the margin recovery next year and the expenses that are going to be rolling off the business?

Edward W. Stack
Chairman & Chief Executive Officer

A

Do we think about them every day? Are we going to come out with anything different than that right now? No, we're going to take a wait-and-see attitude and see how it plays out. With that being said, understand we are aggressively going after this market share. We're aggressively going after this market share to make it as efficient and as much of a flow through as we possibly can, but we think about this every day and are pretty excited about the prospects going forward.

John Kernan
Cowen & Co. LLC

Q

Okay. And then, André, the implied guidance for Q4, how are you thinking about merchandise margin recovery? Obviously, it's very difficult environment in the fourth quarter of last year, promotional all across retail. You lost about 130 basis points of merch margin. How do you think about the recovery opportunity there and what is embedded in your guidance for this year?

Joseph R. Oliver
Chief Accounting Officer & SVP

A

We don't have, I mean, at this point, the guide to Q4 we're not quite there. What I talked about in the comments were more about how we are viewing the full year. So for the full year, so we talked about we expect to see some improvement in gross margin in Q3 as well as the full year, but we haven't guided specifically to Q4 yet.

John Kernan
Cowen & Co. LLC

Q

Okay, thank you.

Operator: Our next question comes from Rick Nelson of Stephens. Please go ahead.

Rick Nelson
Stephens, Inc.

Q

Thanks. I would like to follow up on the footwear deck. You have 117 in place now, 70 more for holiday do you accelerate that rollout now with the big footwear opportunity following TSA's demise?

Edward W. Stack
Chairman & Chief Executive Officer

A

We're looking at what we're going to do next year. We're probably for a while, we're going to read this, we did this in roughly 180 stores, which we think will be our best stores, which includes some new stores. We're going to then sit and read this for most of next year and decide where we want to go after that and see if there's any modifications we want to make to this.

And with what's going on with Sports Authority, we think we've got the time and the patience to be able to do that before we rush and do any more of these, but we're excited about them. We just don't feel that we need to go and add that capital and that expense to the footwear component right now.

Rick Nelson
Stephens, Inc.

Q

Do you envision, Ed, the whole chain producing these decks, or just a small...

Edward W. Stack
Chairman & Chief Executive Officer

A

No. Rick, I don't think it ever gets to be the entire chain. There are some stores that there's not enough term left on the lease. There's some stores that from a volume just don't make sense to put that kind of capital into them. So I don't expect them to be all of them, but I would expect in the next, I kind of go on – I'll go out on a little bit of a limb here. Over the next three years, I would expect that close to half of our stores would have these in them.

Rick Nelson
Stephens, Inc.

Q

Okay, and have you disclosed the lift that you're seeing from these decks?

Edward W. Stack
Chairman & Chief Executive Officer

A

We haven't yet. And it's actually too early to do that. They haven't been in place long enough. We haven't gone through the all-important back-to-school season, get through holiday. So, we haven't yet. We think it's too early to do that.

Rick Nelson
Stephens, Inc.

Q

Okay. Thanks a lot and good luck.

Edward W. Stack
Chairman & Chief Executive Officer

A

Thanks, Rick. Okay, thanks. See you.

Operator: Our next question comes from Patrick McKeever of MKM Partners. Please go ahead.

Patrick G. McKeever
MKM Partners LLC

Q

Okay, thank you. Good morning. Just on the eCommerce, 26% year-over-year growth versus sort of a mid-teens rate for the prior couple quarters. I know you gave some quick drivers in the prepared remarks, but could you elaborate what drove that sharp sequential acceleration? Maybe the month-to-month trend or stronger categories? And I'm also just wondering if you saw any impact from the liquidation sales there, the TSA liquidation sales or from the second annual Amazon Prime Day in July, and some other retailers sort of chasing that event?

Edward W. Stack
Chairman & Chief Executive Officer

A

Yeah, I don't think it was that. I mean, we've done a better job – our team continues to get better. I'm sure we've picked up some business from Sports Authority's online business. Our footwear and apparel business – we continue to be very aggressive in footwear and apparel around the online business, and the Pens and the Cavs winning was also helpful to that business, too. So, it was a little bit of everything. Mostly I think it's that we've done a better job marketing our online business and we've been much more aggressive with our online business and continue – and expect to continue to do so.

Patrick G. McKeever
MKM Partners LLC

Q

So no change in the longer-term, thinking about the growth rate of that business like you had previously maybe said mid-teens or so.

Edward W. Stack
Chairman & Chief Executive Officer

A

Yeah. We'll stay right where we're at for right now. We're not going to guide anything.

Patrick G. McKeever
MKM Partners LLC

Q

Okay, thanks.

Edward W. Stack
Chairman & Chief Executive Officer

A

Thank you.

Operator: Our next question comes from Jim Duffy of Stifel. Please go ahead.

Jim Duffy
Stifel, Nicolaus & Co., Inc.

Q

Good morning. Thanks for taking my question. So I was interested to see your bid for the TSA trademarks and a web domain. Was that a preemptive maneuver? Do you see some potential to use The Sports Authority name and web domain in some strategic capacity?

Andrè J. Hawaux
Chief Operating Officer & Executive Vice President, Interim Chief Financial Officer

A

We clearly see it as a strategic asset for us, and that's why we acquired it, and we're working through plans right now as to how we would deploy that, the intellectual property. As Ed mentioned earlier, the key element of that also was the customer names in the list and how we market to them and how we bring them over to become DICK's customers, but we see that as very strategic for us.

Jim Duffy
Stifel, Nicolaus & Co., Inc.

Q

Okay, and thesportsauthority.com, do you foresee that as an ongoing entity, perhaps a clearance channel for you?

Edward W. Stack
Chairman & Chief Executive Officer

A

We're looking at a number of alternatives to how we might use that. We haven't landed on any particular strategy or tactic yet, but those are some of the things we're talking about.

Jim Duffy
Stifel, Nicolaus & Co., Inc.

Q

Great. I'll leave it at that. Thanks for taking my call.

Edward W. Stack
Chairman & Chief Executive Officer

A

Thank you.

Operator: Our next question comes from David Magee of SunTrust Robinson Humphrey. Please go ahead.

David G. Magee
SunTrust Robinson Humphrey, Inc.

Q

Yeah, hi. Good morning, everybody. Good quarter. I just had one question at this point. With regard to the Olympics, the commercials have been impressive in my mind for DICK's. I'm curious, post the event, can you leverage that into the fall? Do you have any plan to sort of extend the legs of that promotion?

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, we've got marketing plans going into the fall that will be inspirational, the same kind of thought, but they won't be exactly those Olympic spots. We'll be doing something different, but we'll be leveraging what we have always done, and that's focusing on that core true athlete. And whether that's the true athlete that is participating in the Olympics or that really true athlete who is out there running, playing baseball, basketball, doing yoga, we really focus on the authentic side of the business and we'll continue to do so. And I agree with you, our marketing team did a great job with those – the marketing plan around the Olympics. And we've gotten great accolades for it.

David G. Magee
SunTrust Robinson Humphrey, Inc.

Q

Great. Thanks, Ed. Good luck in the second half.

Edward W. Stack
Chairman & Chief Executive Officer

A

Thanks. Thank you.

Operator: Our next question comes from Joe Feldman of Telsey Advisory Group. Please go ahead.

Joseph Isaac Feldman
Telsey Advisory Group LLC

Q

Thanks for taking the question. A lot of mine have been answered, but I did want to go back on eCommerce. Can you just refresh us on kind of what you're seeing within eCommerce? Are you seeing – like maybe the type of products that are sold, or the mix of products, and the customer type. Is it still the loyalty reward member, or is it still the loyalty reward member or is it just a new customer to the company? And just any kind of flavor you can give us about what is selling and how it's being sold it would be great.

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, as we do more and more business online, the business gets to look more and more like what we're doing in the company as a whole. As far as who's shopping there, we're getting new customers all the time. There's a combination of new customers and existing customers, customers who shop online, who shop in the store. It's kind of what you would expect of what's going on with our business online, and I think we're continuing to take market share online from a sports and fitness standpoint.

Joseph Isaac Feldman
Telsey Advisory Group LLC

Q

Got it. And then also online, can you help us think about the profitability of it? I understand where the business is today and that when you take ownership in January next year it'll be more profitable than it is today. But I recall a couple of years ago, you suggesting that it could get to store levels type profitability. And I'm wondering if that's still the case given the changes in the industry and dynamics now with the eCommerce?

Edward W. Stack
Chairman & Chief Executive Officer

A

Yeah, we still definitely think that, and we're getting closer and closer to that every year. We continue to make improvements in that direction.

Joseph Isaac Feldman
Telsey Advisory Group LLC

Q

That's great. That's great. And then just one quick one on the CFO spot. I was just wondering, how are you guys are thinking about that? Is it an external search, internal search, both? And any sense of timeframe when you would like to have somebody, but I know, Andrè, you've done it before and can certainly handle it but you have a lot in your plate. So I'm just curious.

Edward W. Stack
Chairman & Chief Executive Officer

A

Well, we're being very thoughtful about that whether it's external or internal and we're talking with the board. We're going through how best to position this and it won't be long before we have a final decision.

Joseph Isaac Feldman
Telsey Advisory Group LLC

Q

Got it. Great. Thanks, guys, and good luck with this quarter.

Edward W. Stack
Chairman & Chief Executive Officer

A

Great. Thank you.

Andrè J. Hawaux
Chief Operating Officer & Executive Vice President, Interim Chief Financial Officer

A

Thank you.

Joseph R. Oliver
Chief Accounting Officer & SVP

A

Thank you.

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

Edward W. Stack
Chairman & Chief Executive Officer

I'd like to thank everyone for joining us on the call, and we look forward to talking with everyone about our third quarter in a few months. Thank you.

Operator: The conference is now concluded. Thank you for attending today's presentation. You may now disconnect your lines. Have a great day.