28-Aug-2019

Shoe Carnival, Inc. (SCVL)

Q2 2019 Earnings Call

CORPORATE PARTICIPANTS

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

OTHER PARTICIPANTS

Mitch Kummetz
Analyst, Pivotal Research Group

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Gregory R. Pendy
Analyst, Sidoti & Co. LLC

MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon and welcome to Shoe Carnival's Second Quarter Fiscal 2019 Earnings Conference Call. Today's conference is being recorded and it is also being broadcast via webcast. Any reproduction or rebroadcast of any portion of this call is expressly prohibited. Management's remarks may contain forward-looking statements that involve a number of risk factors. These risk factors could cause the company's actual results to be materially different from those projected in such statements. Forward-looking statements should be considered in conjunction with discussion of risk factors included in the company's SEC filings and today's earnings press release.

Investors are cautioned not to place undue reliance on these forward-looking statements which speak only as of today's date. The company disclaims any obligation to update any of the risk factors or to publicly announce any revisions to the forward-looking statements that are discussed on today's conference call or contained in today's press release to reflect future events or developments.

I'll now turn the call over to Mr. Clif Sifford, President and Chief Executive Officer of Shoe Carnival for opening comments. Mr. Sifford, you may begin.

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

Thank you, and welcome to Shoe Carnival second quarter 2019 earnings conference call. Joining me on the call today is Kerry Jackson, Senior Executive Vice President, Chief Operating and Financial Officer. On today's call, I'll provide a brief overview of our second quarter operating highlights and sales results as well as review our fiscal 2019 outlook. Kerry will discuss the financial results in more detail then we'll open up the call to take your questions.

I am pleased to report comparable store sales for the quarter increased 1.4% on top of the 6.7% increase we had for the second quarter last year. This increase was driven by athletics earlier in the quarter and non-athletic as the quarter progressed to a warmer drier seasonal weather pattern. This demonstrates the strength of our model which offers a broad assortment of footwear for any occasion or a season for the entire family.

I'm also pleased to tell you that our back-to-school season is progressing nicely with August sales up 3.5% through yesterday. This increase has been driven through both the athletic and non-athletic product categories. I believe that Shoe Carnival is a shoe store of choice during critical shoe shopping periods. Our customers trust us to have a broad assortment of the best brands and the latest trends.

In addition, I am pleased with very early results related to the initial implementation of our CRM program. I'll speak to this in more detail in a few minutes.

Traffic and average transaction for the quarter declined low-single digits, while conversion increased low-single digits. Average units per transaction were down slightly. We ended the quarter with inventory up 2.3% on a per store basis as we prepared for both the back-to-school selling period and early delivery of fall product.

Merchandise margins were flat to last year. BD&O increased 60 basis points as a percentage of sales and SG&A decreased by 80 basis points. As a result, operating income increased by 20 basis points. EPS for the quarter was $0.80 per diluted share, an increase of 5.3% compared to second quarter last year.

Focusing on the second quarter comparable store sales by department, women's non-athletic was up low-single digits on a comparable basis. We were particularly pleased with the performance of women's dress shoes and sport casuals, both of which produced mid-single digit increases over a comparable basis. Additionally, sandals were up low-single digits. And with the wet and cold start to the second quarter, we experienced high-single digit comp store growth in women's boots.

The men's non-athletic department [indiscernible] (00:04:12) strong performance posting low-single digit comparable store sales increase. Our broad selection of great brands of shoes and boots for any occasion make Shoe Carnival a destination for men's shoes.

The children's shoes department posted a low-single digit increase for the quarter on a comparable basis. We produced mid-single digit increase in non-athletic driven primarily by our seasonal categories. Children's athletic produced low-single digit increase on a comparable basis. We continue to see a shift away from function and more towards fashion in children's athletic footwear. Adult athletic was down slightly on a comparable basis. Here, just like children's athletic, there's been a shift from performance categories to more casual categories.

Now, to update you on the progress on our CRM initiative. We're happy with the continued progress on the CRM implementation and we're also pleased with the early results. Sales to Shoe Perks members for the second quarter were up 5.5% versus last year. This is compared to our 1.4% comparable store sales increase we achieved for the quarter. Gold membership for the year has grown 44% versus last year. This is a key point because the Gold members' average order value is $17 higher than the average order value of our non-Gold members. Segmenting and marketing to members across channels with messaging targeted to specific customers has contributed to this growth.

Additionally, we expect that as we continue to implement our CRM capabilities, we'll continue to grow our active shopper file and convert additional members to Gold status. We have confidence that Shoe Carnival will continue to earn the loyalty of new customers searching for a large selection of footwear for the entire family at a compelling value.

As we move forward, we expect our CRM system to be fully implemented by the end of the fiscal year. Through improved customer analytics, we'll expand our reach to new customers in new and existing markets that closely match the profile of our most loyal customers. As a reminder, this fiscal year, we proactively made the strategic decision to slow store growth as we build our CRM capabilities. Our CRM analysts have begun to provide useful data to both our merchants and our real estate team. With this insight, we fully expect to continue to drive profitable sales growth in our comp stores and once again began to expand our brick-and-mortar footprint beginning in fiscal 2020.

For the second quarter, we ended with 393 stores in 35 states in Puerto Rico. During the quarter, we closed two stores and had no new store openings. For the remainder of the year, there is one new store plan and two additional store closures.

Finally, I'd like to give you an update on our financial expectations for fiscal 2019. As I've said earlier, back-to-school has gotten off to a good start with August sales month-to-date up 3.5% versus the same time period last year. Comparable store sales for the past two years in August have increased 7% and 6.5%, respectively.

This August will represent the 17th consecutive year with positive comparable store growth for the month. I'm happy to share that our August comparable store sales increase has been driven across all channels and all major product categories. I am especially pleased with the increase in traffic our brick-and-mortar stores are experiencing.

Our customers count on us for an unparalleled shopping experience. Shoe Carnival combines a fun store environment with the latest brands, trends and key styles at a compelling value. Based on our performance year-to-date, we feel comfortable maintaining the high end of our annual diluted earnings per share guidance of $2.83 and raising the lower end of the range to $2.77. This compares to diluted earnings per share of $2.45 in the prior fiscal year.

With the first half of the year complete, we are refining our net sales estimates while maintaining our comparable store guidance for the year at a low-single-digit increase. Total sales for the full fiscal year are expected to be in the range of $1.028 billion to $1.033 billion.

That concludes my overview. I'd now like to turn the call over to Kerry.

W. Kerry Jackson

Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

Thank you, Cliff. Our net sales for the second quarter ended August 3, 2019 of $268.2 million were essentially consistent with the prior-year second quarter. Our comparable store sales increase of 1.4% contributed $3.6 million to net sales and $1.2 million was attributable to the three new stores opened since the beginning of the second quarter of fiscal 2018. These increases were offset by a loss in sales of $3.7 million from the 15 stores closed over the same period and a loss in sales of $1.2 million attributable to other non-comp stores relating primarily to hurricane-impacted stores.

Our gross profit margin for the quarter was 30.6% compared to 31.2% in the second quarter of last year. Our merchandise margin was flat for the quarter while buying, distribution and occupancy expenses increased 60 basis points as a percentage of net sales. The increase in buying, distribution and occupancy expenses as a percent of net sales was primarily a result of lower occupancy expense in Q2 of last year. This was due primarily to a $1 million lease termination benefit in that prior-year quarter for two stores in Puerto Rico where the landlord could not make contractually required repairs within the allotted time. Also contributing to the deleveraging of expenses was a slight decline in sales for Q2 against higher expenses.

SG&A expenses decreased $2.4 million in the second quarter of fiscal 2019 to $66.4 million. As a percentage of net sales, these expenses decreased to 24.8% compared to 25.6% in the second quarter of fiscal 2018. The decline in our SG&A expense in Q2 was due to lower equity and incentive compensation. In Q2 last year, we tripled our quarterly earnings, resulting in an increase in incentive and equity compensation expense of $4.8 million. A more moderate increase in Q2 earnings this year resulted in a $3.9 million reduction in incentive and equity compensation expense as compared to the prior-year period.

Other significant changes in SG&A for the second quarter of fiscal 2019 included a $1.2 million decrease in depreciation expense and a $0.8 million decrease in expense for stores that have closed or are closing, net of new store expenses. These decreases were offset by a $1.6 million increase in payroll expense and a $1.4 million increase in advertising expense.

The effective income tax rate for the second quarter of fiscal 2019 was 24.5% compared to 21.6% for the same period last year. For the full year of fiscal 2019, we expect our tax rate to be approximately 21% compared to 24.3% last year. The reduction in the annual tax rate this year was a result of a $1.9 million tax benefit related to vesting of equity-based compensation in Q1 this year.

Net income for the second quarter was even with last year at $11.8 million or earnings per diluted share for Q2 increased $0.04 to $0.80 per diluted share. Weighted average diluted shares outstanding for Q2 this year decreased 4.1%.

Now turning to our cash position and information affecting cash flow. Depreciation expense was $4.1 million in the second quarter. Depreciation expense is projected to be approximately $16 million for the full fiscal year.

Capital expenditures for fiscal 2019, including actual expenditures during the first half of the year, are expected to be between $21 million and $22 million, with approximately $16 million to be used for new stores, relocation, remodels and the purchase of our corporate headquarters. The remaining capital expenditures are expected to be incurred for various other store improvements, normal asset replacement activities and continued investment in technology.

Similar to Q2 last year, we did not repurchase any of our common stock during the second quarter this year. We continue to expect diluted weighted average shares outstanding for the fiscal year to be approximately 14.7 million shares. We currently have $36 million available under our $50 million share repurchase authorization.

My final comment today will focus on adding a little color on our earnings expectations for the third quarter this year. At the high end of our annual earnings guidance, we expect Q3 comparable store sales to increase low-single-digit. Our merchandise margin is expected to be flat to slightly up. Buying, distribution and occupancy expense should leverage moderately due to lower distribution costs and SG&A is expected to be flat to slightly up as a percentage of sales.

This concludes our financial review. Now I'd like open up the call for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] And we'll take our first question from Mitch Kummetz with Pivotal Research. Please go ahead, sir.

Mitch Kummetz
Analyst, Pivotal Research Group

Q

Yes. Thanks for taking my questions. Cliff, could you elaborate a little bit on the athletic business? It sounds like for the quarter it was maybe better early than late and that just is a little counterintuitive to me, just given that your biggest athletic vendor was flowing a lot of new product late in the quarter. And also you made some comments about there's a shift in athletic to more casual, which again seems to kind of go against what I would think would be the benefit of that vendor flowing in that newer product. So just a little more color on athletic I think would be helpful. Thanks.

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

No problem, Mitch. You are right that our largest athletic vendor did flow in new product as we went through the quarter. But most of that product came in towards the tail-end of the quarter, so it didn't have a major effect as a whole in the second quarter. I think you know what I'm talking about when I mentioned casual athletic has been a major contributor for the quarter. Everyone knows what's going on with the skate category right now.

Mitch Kummetz
Analyst, Pivotal Research Group

Q

And then, Kerry...

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

I will add this that as we moved into back-to-school, we saw increases happen, I mentioned this in my prepared remarks, throughout all product – most major product categories and very happy with that. So you're getting a lot of sales from women's canvas product, men's canvas product, skate and [indiscernible] (00:16:53) what you would consider to be true athletic product.

Mitch Kummetz
Analyst, Pivotal Research Group

Q

Okay. That's helpful. And then Kerry, on the sales guide, so you've down the sales guide for the year, no change in the comp outlook. It looks like you're closing fewer stores. So, is the reason the sales guide comes down because you're now not expecting a lot of volume from liquidating those stores? Is that really the difference on the sales guide?

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

No, the difference really came out in the first half. Now that we've actually gone through it and we can adjust to actual – the annual guidance we had at the beginning of the year against where we are mid-year, which is why we adjusted the earnings or the sales down. But we still feel confident in our earnings expectations as we've been able to make adjustments throughout the year to compensate for a little lower sales than we originally expected.

Mitch Kummetz Q
Analyst, Pivotal Research Group

And then maybe lastly, Cliff, on Payless. I think the thinking going into the quarter was sort of net neutral for the quarter or maybe a little bit of a drag early, but then a benefit late. I'm hoping you could maybe speak to kind of what you saw in those stores that overlap with Payless in the quarter?

Clifton E. Sifford A
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

We have not seen a lot of change in those stores from an overall base, they comp pretty close to what's the company comp. But you got to remember, there are a lot of shoes that were liquidated early in the quarter at least through the first half of June and that took up a lot of the open-to-buy, customers open-to-buy, so to speak, and I think we'll see the benefit of Payless going away as we move through the third quarter.

Mitch Kummetz Q
Analyst, Pivotal Research Group

Okay. All right. Thanks, guys.

Operator: And our next question comes from Sam Poser. Please go ahead, sir.

Sam Poser Q
Analyst, Susquehanna Financial Group LLLP

Good afternoon. Can you just tell us what you're – the comps, like, what you were up against by month and last year in the second quarter and then what you're up against by month? You mentioned 7.5% in August of 2018. Can you just [indiscernible] (00:19:20) September and October look like?

Clifton E. Sifford A
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

Yes. Kerry is getting that for you now, Sam. As you'll remember, we had a strong second quarter last year.

W. Kerry Jackson A
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

Sam, last year, the second quarter started May up in the low teens and then June was up high-singles and then July was down low-singles.

Sam Poser Q
Analyst, Susquehanna Financial Group LLLP

And then September, October or August, September, October?

W. Kerry Jackson A
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

August, we've talked about, was up 6.5% last year. And then we saw both September and October being up low-singles.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

So when you think about no Payless and your overall product mix, how do you view – do you view Q3 being a better – like, a bigger number than Q4 as far as a comp increase? I mean, is that how we should think about it or do you think they're looking fairly aligned as far as the comp increase given the good start?

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

I think they look fairly aligned even given the good start as we move through third quarter and fourth quarter.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

And I assume based on the start that you have and no Payless that you would anticipate the back half of the comp in Q3 and Q4 to be better than the comp in Q2?

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

Yes, that is correct.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

Fair. That's a fair...

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

I think that's a fair statement.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

And then your sandal business was a little different than somebody else recently. Can you talk to us about what kind of things worked in sandals? What type of product work and maybe didn't work in your sandal [ph] category (00:21:30)?

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

Well, it wasn't surprising. We mentioned in the last call that we thought we were going to get comp store growth out of sandals. So we weren't surprised by that, but we did see continuing improvement in footbed sandals as we move through the quarter and wedges as we move through the quarter – long wedges as we move through. So, I'm happy that [ph] when they're (00:21:56) up low-single, so I can't tell you we blew the doors off, but I'm very happy with the fact that sandals comped positive in the second quarter.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

But, I mean, that was probably the story of like mid-single-digits down at the beginning and then better than mid-single-digits...

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

That's exactly...

[indiscernible] (00:22:14)

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

Sam, that's exactly what happened is that we started the quarter down, and we had faith that as we move through the quarter, we'll see increases. And we did. And, by the way, I just want to reiterate that we saw those increases. Our margin for the quarter and sandals improved over last year. So, it wasn't the fact that we were clearing through.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

I know that you don't like to talk about brands, but, I mean, one of the big brands and one of your biggest brands was Nike and you talked about – there's been a lot of talk in the athletic space about the improvement of the Nike product for your channel. Can you sort of give us some idea of how that's shaping up and how you see that overall sort of through the balance of the year, maybe even in the next year now that you've seen that product? And then lastly, you haven't mentioned the tariffs at all. Could you give us some view of sort of any impact of the tariffs that you've built into your guidance or how you're thinking about all that? Thank you.

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

I'm going to live with my commitment not to talk about brands on the call. So I'm going to skip that question. I will tell you, as I've said on the last call and I still believe that is that the product has gotten better as we've moved through the second half of the year and we expect it to continue to [indiscernible] (00:23:50) all the products we've seen as we move through the rest of the year we're happy with and that's the extent of which I'm going to talk about brands.

From a tariff standpoint, we built whatever tariffs we felt were going to hit us into our guidance. However, we don't believe that we're going to – about 10% of the product that we're importing on our own will be affected by the 9/1 tariffs, so very small portion. As you know, we only do about 20% of our women's business and about 30% [indiscernible] (00:24:31) about 10% of our kids business are direct imports. Kids is driven so strong by athletic. So, very small percentage of our receipts for September are going to be affected.

The rest, for the 12/15 tariffs, we have arranged to have most of that product, the vast majority of that product deliver prior to 12/15. So we don't see any [indiscernible] (00:25:04) very, very little impact to our margin for this year on tariff, Sam.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

And what about the brands, I mean, and how they're handling it and how you maybe think pricing for next year? I've heard one of the large...

[indiscernible] (00:25:19)

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

...that we've already started to hear that there are some price increases going on in kids.

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

I can tell you that as of today we have not seen any price increases in kids or in adults.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

Thank you very much and continued success.

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

All right. Thank you.

Operator: And our next question comes from Chris Svezia with Wedbush. Please go ahead.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Good afternoon, gentlemen. So I want to go to the revenue outlook. Kerry, could you just walk through that one more time? What has changed in your view to kind of walk back a little bit the revenue outlook [indiscernible] (00:26:11) just – I don't know just add a little more color about why that change, what you saw relative to your plan that changed that revenue outlook?

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

Well, it was primarily just truing up our expectations to first and second quarter actual results. If you remember, in Q1, we talked about we had a difficult February and our comps were down high-single-digits. We were expecting a little bit of a rebound. And while we didn't true up our sales effect at that point in time when we announced our Q1, it appears that whatever happened in February never rebounded on.

So if you remember we came back with a decent Easter on a combined March and April together was up high low-single-digits, which was comparable last year. So that effect we ended up truing that up. We also had a little bit difficult during the Mother's Day area in May and those two factors were the primary factors of truing up what our original expectations in the first half were to what we now expect. We really have not adjusted our second quarter outlook from what we originally expected for the year. This was just truing up the actual.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay. Got it. That's helpful. And then just I want to go to your guidance that you've given, kind of a preliminary walk-through here for the third quarter. Based on rough math, that would imply, call it, the upper end of the range somewhere in the $0.12 to $0.14 for the fourth quarter. Maybe just walk through some of your thought processes to sort of the acceleration or the material improvement in earnings for that period? Just remind us what some of the puts or takes, maybe closing fewer stores, less liquidation sales, just on a thought process to kind of kind of get to that number.

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

Well, if you really look at it, it's going to be an increase in sales and you're really talking about the fourth quarter, I think, you're saying, right?

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Right.

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

A slight decline in the gross profit margin and will leverage your expenses fairly significantly because we won't have as large expense for incentive and equity compensation. Similar to what we saw in Q2, we're going to see a savings in our overall SG&A. I'd expect to see less SG&A expense for the quarter and fourth quarter this year versus fourth quarter last year. That would lead you to the increase on a year-over-year basis.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Got it. Okay. And I want to go back just to comp drivers for a moment. I know you don't want to talk about brands, but let me ask it this way. Could you get to a 3.5% comp in August without your largest brand comping positive?

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

That is...

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

That's good [indiscernible] (00:29:34).

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

Chris, that is a terrific question, which I'm not going answer...

[indiscernible] (00:29:40)

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

You can't tackle that. Come on. And the answer is...?

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

I'm sorry. I must have not heard your question. When I said I wasn't going to answer the question, what did you ask?

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Oh, you're not going to answer my question even if I ask [indiscernible] (00:30:03)

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

If I answer [indiscernible] (00:30:06) it really goes against my policy of talking about brands. And the story of the day is we're up 3.5% for the month of August and, to me, that all is driven by the fact that the merchants have done an incredible job of delivering great product to our stores, our stores have done terrific job of selling that product. And I just don't want to get involved in and talking about individual brands. And so I'd like to leave it at that.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay. I tried. I want to ask you about boots. Since, I guess a couple of months ago versus today, any change in your thought process about the fashion business as it plays out to the back half of the year?

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

We actually feel pretty good about the boot business as it plays out in the second half and I believe we'll see a strong [ph] booty (00:31:11) component early and I hope really don't want to talk too much about the types of products I think we'll sell in the fourth quarter just from a competitive environment standpoint. But we feel pretty good about boots.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay. Do you feel better than you did, call it, three months ago?

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

Three months ago, I didn't see the entire selection. Since that time, the buyers have walked – both Carl and I through that program, we know what the advertising cadence is. So, yes, I feel better today about our boot opportunity than I did three months ago maybe because I'm more educated on it than I was three months ago.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Well, that's good to know that you're better educated on it. Last thing, I have here is just on the buyback. So, Kerry, just give me your thought process. I know you initially have said you bought back what you thought you would have, I think in the first quarter for that period. Are there some logic about the planning of the buyback and you had done more than you had thought or planned to earlier? [ph] Just thoughts why you've been buying back stock here (00:32:31) was it just the inventory commitments for back-to-school, et cetera and just any color you can add about how we should think about for the balance of the year? I know you [indiscernible] (00:32:40) 14.7 million shares, but just any thoughts around it would be helpful?

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

So, we wanted to help you understand where we're at. So we're maintaining our thought of where we're going to end the year with diluted average shares outstanding, so that hasn't changed. We didn't buy any shares in Q2 last year. It's just either – we really have two factors. When do we feel that there is a value in our stock that we want to buy it back; and secondly, we'd monitor – when we always do it only through excess cash. Q2, because we're building up our inventories, and at the end of Q2, we always have the highest – typically, we always have the highest inventory levels of the year. So, we're building up our inventories throughout the quarter which is, it takes a lot of capital commitment. Typically, that's the lowest free cash available during the quarter. So, those are the factors that we play into when we said we'd do buyback or not.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay. So, in the balance of the year, the outlook, you're just assuming no additional share repurchases though should the opportunity present itself, you would obviously be more aggressive in [ph] buying stock – stock there(00:34:00)?

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

No, we actually, [ph] because – (00:34:02) we get very cash flow rich at back-to-school because August is such a large quarter, we liquidate those inventories. And we don't have a large inventory build throughout the rest of the year. So we have factored in purchases in our guidance through in the second half.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay. I'll leave at that.

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

And that'll be dependent – so I see it less of an issue of free cash flow being an issue that would restrict what quarter we buyback, but it'd be dependent on the price and if it represented a value.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay. Okay, that's all I have. Thank you very much, gentlemen.

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

Thank you.

Operator: [Operator Instructions] We'll take our next question from Greg Pendy with Sidoti. Please go ahead, sir.

Gregory R. Pendy
Analyst, Sidoti & Co. LLC

Q

Hi, guys. Thanks for taking my question. I just wanted to dig into the trimmed store closure count and if you can kind of give us any color on maybe what was behind that, was that lease opportune – more attractive lease opportunities. You said earlier you completed your CRM project, kind of any insights there or was it just kind of reduced competition? Just any color on what kind of brought that down a bit?

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

Well, we always work with our landlords and we look at the current – the most recent trends with the store and if a store's improving and we can get some relief on the cost structure, we can extend stores [ph] to into (00:35:39) future periods and that's what – that's basically what we did. We were able to find – have a store to meet metrics that would meet our criteria for keeping it and maybe extending a year or two while it continues to see if we can continue that positive sales trend we saw prior to the extension.

Gregory R. Pendy
Analyst, Sidoti & Co. LLC

Q

Okay. That's helpful. And then just on that subject. Just one final one, are you still planning to pivot to net store growth in the following year?

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

Yes, we are. It's going to be a very moderate net store growth based on our outlook. Now that outlook could change as with the economy right now, the big talk-in in all the financial press is a recession. If we see a recessionary environment where we saw the consumer pullback, we would adjust our thought processes going forward on that. And in fact it might slow down, the amount of stores we might open and it may require us to increase the number of stores we close. So it's hard to predict at this point in time, but we are in line with what we said in previous quarters that we see small net store growth.

Gregory R. Pendy
Analyst, Sidoti & Co. LLC

Q

Got it. That's helpful. Thanks a lot.

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

Thank you.

Operator: And we will take a follow-up question from Sam Poser with Susquehanna. Please go ahead.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

Hi, guys. I just want to follow-up on Chris' question. Let me rephrase it. Can you hit a 3.5% comp in the quarter without athletic being up as a whole? Because that's the biggest chunk of business. I mean it's over 50%...

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

What was that question?

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

So can you do that? Can 54% of your business be down and you still be comping a 3.5%. Is that reasonable given the trends?

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

That is reasonable to assume that we – if athletic were comping down, we would have a tough time hitting the 3.5% comp.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

And since this unknown vendor is the largest part of athletic, it would be unlikely that that business is down to get you to the 3.5% comp if we follow the logic. Am I following this correct?

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

You need a comp in athletic – you need to have positive comps in the athletic to post a 3.5% comp.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

Okay. Thank you. And then Kerry, just to the store question, if this chatter about a recession is true, wouldn't that also lower theoretically lower the rents and lower the leases and give you sort of a big opportunity to step in and open stores for when the dust settles? And to renegotiate leases to better rates that could keep more stores open? Now that you're doing all this now with the CRM and all this other stuff rolling out that should make your business more efficient sort of in the larger picture?

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

Well, Sam, that's a very logical way of looking at it. What we've seen in the past is that, it didn't actually happened that way. Prior to the last recession, we had the same thought process that we would – we would be getting a lot of opportunity for store growth because there would be more boxes available. The [ph] rents (00:39:26) would be much more cost-effective. What in practice we saw is that the landlords had so many retailers coming back to them asking for rent relief that it really hardened in that the negotiation and that unless you had a lease event where you could actually say, I'm going to kick out of this lease or I'm not going to renew it, they wouldn't even talk to you. So, they were having to prioritize who they talk to. So, we're going in – we're – we won't go into any type of [ph] tough and (00:40:03) retail environment or economic environment with that thought process again. If it turns out to be different this time, we could reevaluate. But based on past history, those opportunities aren't available.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

And what percent of your store base is on lease that would be on lease expiration or kick-outs next year?

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

Up until recently, we've been a fairly ratable grower on a year-over-year basis. So, 10% or greater of our leases would come up each year.

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

And, Sam, I think you can tell by the fact that each year, the past three years, we've lowered the expectation of the number of stores that we were going to exit, and that is due to several reasons. One is the increasing sales and the stores begin to perform. Two, we were able to get better deals through the landlord and thus the stores became more profitable for us. So, we continue – we work on that almost every day. So – and that's the reason why the expectation of the store closures have continually gone down.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

So I understand. I mean I guess the question is though that we've – you've got no more Payless which is a whole ton of stores then – and you have your CRM and your communication which apparently is improving and making more Gold customers and so on, and your net opening next year is I mean it's not going to be very much. So why – give sort of the offset of Payless and the internal improvements why would – I mean I don't even – I mean why would you go from small net openings to net closings in a situation like that when you take into account those other factors or is this just you're being prudent in the way you're asking the question just in case you get to net closings next year.

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc.

A

Well, there's a significant amount of time for us to evaluate that from what you're saying about the CRM coming online, getting the usage of it, understanding how much of a benefit that's going to be, how immediate that's going to be. We typically don't set the out-year goals at this stage beyond what we have visibility on and right now that's where we have visibility on. There may be greater opportunity and we could capitalize on it, but at this point in time we don't see that.

One thing we should say also is that we're not going to be going into any new markets which – so for the next several years or more we have opportunities to backfill the markets. We have to make them more productive where we already have brand awareness or where we can continue to build additional brand awareness. So that would be the prudent way for us to grow and by that by itself will limit opportunities.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

Do you have any leases signed for next year yet or is that all work in progress for these new locations?

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

A

We have several [indiscernible] (00:43:34) if they're not signed, they're near – they're near. So I couldn't say for sure.

Sam Poser
Analyst, Susquehanna Financial Group LLLP Q

And I assume that that's more stores whatever are near is more stores than you're planning to open this year based on what you – based on your current number?

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc. A

That is correct.

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc. A

Yeah.

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc. A

Our belief, we only believe we'll open one store this year.

Sam Poser
Analyst, Susquehanna Financial Group LLLP Q

Thank you, guys, again. Appreciate it.

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc. A

Thank you, Sam.

W. Kerry Jackson
Senior Executive Vice President, Chief Operating and Financial Officer & Treasurer, Shoe Carnival, Inc. A

Thank you, Sam.

Operator: And it appears that is all the time that we have for questions and answers for today. Mr. Sifford, I would like to turn the conference back to you for any additional or closing remarks.

Clifton E. Sifford
President, Chief Executive Officer & Director, Shoe Carnival, Inc.

Thank you. And thank you for joining with us today, and we hope you have a very enjoyable Labor Day weekend, and we look forward to talking to you about our third quarter results in November.

Operator: And this does conclude today's call. Thank you so much for your participation. You may now disconnect.