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DECK - Q2 2013 Deckers Outdoor Corp. Earnings Conference Call

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OVERVIEW:

DECK reported 2Q13 diluted loss per share of $0.85. Expects full-year 2013 revenues to increase approx. 8% over 2012 levels. Expects 3Q13 revenue to increase approx. 2.5%. Expects 4Q13 revenues to increase approx. 14.5%.

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PRESENTATION

Operator

Good afternoon, ladies and gentlemen, and thank you for standing by. Welcome to the Deckers Outdoor Corporation second-quarter fiscal 2013 earnings conference call. At this time, all participants are in a listen-only mode. Following the presentation we will conduct a question-and-answer session. Instructions will be provided at that time for you to queue up for questions. (Operator Instructions). We would like to remind everyone that this conference is being recorded.

Before we begin, I would like to remind everyone of the Company's Safe Harbor policy. Please note that certain statements made on this call regarding the Company's expectations, beliefs, and views about its future financial performance, brand strategies, and cost structure are forward-looking statements within the meaning of the federal securities laws. These forward-looking statements are intended to qualify for the Safe Harbor from liability established by the Private Securities Litigation Reform Act of 1995.

These statements relate to the Company's anticipated revenues, expenses, earnings, gross margins, capital expenditures, brand strategies, and cost structure as well as the outlook for the Company's markets and demands for products. The forward-looking statements made on this call are based on currently available information and, because its business is subject to a number of risks and uncertainties, some of which may be beyond its control, actual operating results in the future may differ materially from the future financial performance expected at this current time.

Deckers has explained some of these risks and uncertainties in its earnings press release and in its SEC filings, including the risk factors section of its annual report on Form 10-K, and on its other documents filed with the SEC. Listeners are cautioned not to place undue reliance on forward-looking statements which speak only as of the date hereof. The Company undertakes no obligation to publicly release or update the results of any revisions to forward-looking statements.

I would now like to turn the conference over to the President, Chief Executive Officer, and Chair of the Board of Directors, Mr. Angel Martinez.

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

Thank you to everyone joining us today. With me on the call is Zohar Ziv, Chief Operating Officer, and Tom George, Chief Financial Officer. In addition, I would like to introduce Linda Pazin, our new VP of Investor Relations and Corporate Communications, who is also on the call.

The second quarter, while our smallest volume quarter, was an important transition period for the UGG brand, but it left us feeling much more confident about our growth prospects in the back half of the year than we felt 12 months ago. The transitional product we have developed to help better bridge the gap between spring-summer and our key fall holiday season was very well received by our [retail] consumers, our customers and the initial styles that were introduced late in the second quarter have performed very well at major wholesale accounts and in our direct-to-consumer channel month to date.

The quality of our inventory, which I will address in more detail in a moment, is in much better shape both in the channel and in our distribution centers. It is much cleaner than a year ago and we have the key fashion styles on hand to deliver on time in early August versus last year, when factory delays meant these important transitional products didn't arrive on the shelves until late September.

And we believe that the combination of solid spring sell-through, more compelling, more relevant product collections, and much improved in-store merchandising has created far better momentum across each of our regions and distribution channels at the start of this year's third quarter versus what we experienced in 2012 when we were battling several headwinds beyond our control.

Despite pressure on our Teva and Sanuk brands sandal business from cold and rainy weather during large durations of Q2, we were able to achieve sales within 2% of our guidance. Additionally, our second-quarter revenue was in line with guidance on a constant currency basis. We reacted quickly by deferring certain expenses, primarily marketing, selling, and retail dollars, to the back half of the year to take better advantage of the big year fall selling season, which enabled earnings to exceed expectations.

The second quarter ended with inventories up 4.6% year-over-year, a growth rate is much more aligned with sales trends than in the previous several quarters. While this was a positive development, inventories were higher than we originally anticipated, driven mostly from a timing issue from us accommodating factory requests to take some small fall deliveries ahead of schedule so they can better be prepared for their peak production period. This product will be utilized to fulfill early season demand of key wholesale accounts and our expanding direct-to-consumer channel, which includes 36 more stores compared to this time a year ago.

Slower than originally planned first half sales for Teva and Sanuk contributed slightly to our inventory growth, but we expect to work down this excess inventory over the remainder of the summer. While we are comfortable with the quality and size of our inventory as we head into our key selling season, we plan to continue to focus resources to improve the flow and timing of inventory receipts. We recently hired a new senior executive in supply chain planning, who we believe will add significant improvements to tracking and management of our order status with factories.

I think it is also important to note that this management team has a very good track record of turning inventory and while our level of carryover for the past two years has been higher than usual due to -- in part to back to back mild winters, history shows that we have not needed to write off or write down significant inventory at any point and we believe that this will continue to be the case going forward.

Looking at the brands' recent performances in more detail, starting with the UGG brand, while domestic wholesale selling was down modestly, the UGG brand's US wholesale customers experienced good sell-through of the spring line led by the Kfar espadrilles collection, fashion sandals, specialty spring classics, and slippers. This followed a very good Q1 during which cold, snowy weather in many parts of the country helped drive additional sales of classic boots and other colder weather socks.

Demand for spring styles as well as new transitional products such as driving mocs, smoking slipper silhouettes, ballerinas, and trend-right sneakers, which were introduced late in the quarter, helped drive another strong quarter for our domestic e-commerce business.

Our digital marketing programs are using significant year-over-year traffic increases through UGGAustralia.com. These styles performed in our concept stores as well, specialty classics such as our new Josette boot and the companion handbags performed well early and slippers continue to sell year-round online and in the concept stores.

Our recent market research has reaffirmed our belief that the UGG brand remains a top-tier brand relative to the competition. Approximately 80% of women in the US are aware of the brand, over 40% have considered buying the brand, and about 20% have purchased the brand -- 25%, sorry, have purchased the brand. This places the UGG brand in the top five in their peer group in the competitive female category. This is great news and we believe it reflects the strength of the UGG brand as they gear up for their fall marketing campaign supporting their 35th anniversary.

In terms of our domestic retail performance, comps were down 10% on top of a mid single-digit increase a year ago. The comp decline was merely a function of traffic, which we believe was primarily due to weather and our decision to run our spring digital and out of home advertising campaign in Q1 this year versus Q2 last year, as the first quarter is a much bigger period for retail.

A shift in product mix toward lower average selling price product, including slippers and casual shoes, also weighed on comps. A decline in comparable transaction in the quarter was partially offset by an increase in units per transaction, which translates into more consumers experiencing the UGG brand. As we continue to develop our omni-channel strategy, we are pleased that in the US on a combined basis our direct-to-consumer business was up approximately 14% as our operational initiatives to drive conversion took hold.

Moving on to our European business, many wholesale customers in the UK, our largest market outside the US, experienced their best spring selling season ever with the UGG brand. Their performance earlier in the year was driven by cold temperatures, including the coldest March in the UK in more than 50 years. As weather warmed towards the end of the second quarter, sales of non-boot spring styles such as flip-flops, fashion sandals, and espadrilles accelerated.

What we experienced in our UK wholesale channel was also true of our direct-to-consumer business. Stronger first-quarter results driven by cold weather were followed by slightly softer Q2 results as sales of non-boot spring styles didn't pick up until temperatures warmed later in the quarter. Comps in the UK were flat for the quarter.

Our UK results so far this year are encouraging and we have a long way to go in building added confidence. We've gone a long way as well in building added confidence in the long-term viability of the UGG brand in this very important market. And you will remember that we have faced some challenges in the last few years, we have overcome those and the consumer is responding very positively to the brand in the UK. Now we have to make sure we capitalize on this momentum while also replicating our progress in continental Europe where conditions continue to be more challenging.

The results also show strong correlation between sales and whether in Europe, highlighting the need for more transitional and non-seasonal product, something we are addressing in all of our markets.

Now to Asia-Pacific where the UGG brand continues to demonstrate great momentum, particularly in Japan. Our retail stores comped up in the mid-20% range, driven by a positive response to this year's spring line. Comps in China were down mid-single digits, a marked improvement from recent quarterly trends, which we believe is attributable to the new merchandising and marketing initiatives that we've recently implanted.

We continue to believe that the Asia-Pacific region -- and I'm not just referring to Japan and China -- offer significant opportunity for the UGG brand and we are moving quickly but purposefully to capitalize on the prospects we have identified in each country. In addition to the seven stores we expect to add in Japan and the 15 new stores we expect to add in China, there will be multiple partner stores by year-end in all of the regional distributor markets for the UGG brand including South Korea, Taiwan, Mongolia, Singapore, and Australia.

Turning to the Teva brand, sales were down year-over-year as reorders didn't materialize to the levels we expected given the unfavorable weather. Our sandal sales, which declined in line with the industry, were partially offset by gains in our closed toe category. As mentioned on prior earnings calls, we continue to focus on transforming the Teva brand into a more complete outdoor footwear brand in order to increase its growth prospects and lessen its dependency on weather.

Our new Teva sphere technology will be expanding with new color updates for fall. In addition, we are introducing two new casual styles for men into new boot collections for women, one of which, the Capistrano, is being given platinum level marketing designation by our number one retailer, REI, which is a first for the brand.

Before I turn to the Sanuk brand performance for the quarter, I wanted to remind everyone that the Sanuk brand started off as a predominantly male one-season surf brand when we acquired them in 2011. Now we are transitioning the Sanuk brand into a lifestyle brand that will be featured in department stores, sporting goods, and outdoor retailers in 2014. I'm very excited about the product that's been developed for the female consumers and that will be featured in our spring 2014 line.

These changes are an important part of the growth story for the Sanuk brand. Sanuk brand sales, while up 7.5% for the quarter, were also hampered by cold, rainy weather throughout much of the quarter. There were pockets of strength, particularly our direct-to-consumer channel, which was up over 80%, driven by the continued strong performance of our e-commerce site and the addition of the brand's first store, which opened in Santa Monica earlier this year.

We are encouraged that the brand's sandal sales outperformed the industry average this season driven by solid sell-through particularly in our women's yoga mat franchise at core independent retailers and department stores. We expect the brand will gain momentum in the second half of the year based on several new product introductions.

Fall 2013 represents the first time we'll have sidewalk surfer styles in men's and women's that are relevant during the critical transition from summer to fall and holiday. We are also building off the success of our Chill collection with updated styles that are lighter weight to allow sidewalk surfer-loving customers the ability to wear their favorite style deeper into the year.

You will also see new boots from the Sanuk brand, including more women's silhouettes in feminine colors and patterns. We believe that our R&D efforts will transition the brand from primarily a hanging footwear merchandise brand to a meaningful player on the footwear wall in our surf outdoor and footwear specialty channels, during what has traditionally been the brand's off-season.

I will now turn the call over to Tom for a deeper review of the numbers and an update on guidance.

Tom George - *Deckers Outdoor Corporation - CFO*

Thanks, Angel. Today's earnings release contains a good amount of detail about our second-quarter sales and earnings including sales by brand channel and geography. Therefore I'm going to limit my discussion primarily to gross margins, operating expenses, the balance sheet, and guidance.

Gross margin for the second quarter was 41.1% compared to 42.2% in the second quarter of last year. The 110 basis point decline was primarily attributable to higher closeout sales combined with higher cost of goods sold that was a result of increased sheepskin price that we locked in at the end of September 2011. The benefit of last year's lower sheepskin costs won't be realized until late Q3 or early Q4 this year.

Total SG&A expense for the quarter was $112.6 million or 66.2% of net sales compared to $102.3 million or 58.6% of net sales a year ago. The dollar increase versus a year ago was primarily due to approximately $10 million of additional expense related to our retail operations, most of which is for the 36 new retail stores that were not opened during the second quarter last year as well as higher performance-based compensation expense, partially offset by a decrease in Sanuk earn-out accretion compared with a year ago.

Operating loss for the second quarter was $42.8 million compared to an operating loss of $28.7 million last year. The decline in operating margin was a result of a decline in gross margin combined with the increase in SG&A as a percent of sales.

We recorded an income tax benefit of $13.8 million in the second quarter compared to $8.4 million in the second quarter last year. Second-quarter diluted loss per share was $0.85 versus $0.53 a year ago and compared favorably to our guidance for a loss of approximately $1.10. The upside relative to our guidance was driven primarily by lower operating expenses of approximately $11 million, approximately $5 million of which we shifted into the back half of the year to take better advantage of the busier fall selling season.

Regarding our retail operations, for all stores open at least 12 months at June 30, 2013, the average sales per square foot was approximately [$]1,500 in total square footage. At the end of the second quarter was approximately 241,000 square feet compared to roughly 139,000 square feet at the end of the second quarter 2012, representing an increase of about 70%.

Turning to the balance sheet, at June 30, 2013 inventory increased 4.6% to $362.1 million from $346.3 million at June 30, 2012, an increase of $15.8 million. UGG brand inventory increased modestly by $2.5 million or 0.8% to $311.4 million to support the current wholesale order book as well as our DTC business growth. In addition, the balance included early deliveries of new transitional and fashion product for fall 2013 as well as approximately $11.2 million is due to 36 more retail stores compared to a year ago.

We were pleased with the quality of the UGG brand inventory as in line and carryover products represented approximately 90% of UGG brand inventory. The remaining 10% is inventory either in or available for our outlets.

Regarding orders for in-line and carryover product as of June 30, we have more orders than we have inventory. So in Q3 and Q4 we are expecting additional inventory to fulfill our wholesale order book as well as our DTC business, which has grown to over 30% of our business. In addition, we will have inventory of key styles available for reorders from our wholesale customers.

With regard to our other brands, Teva brand inventory increased $3.8 million to $24.9 million and Sanuk brand inventory increased $5.1 million to $14.4 million as a result of lower-than-expected sales for the first half of the year. Our other brands inventory increased $4.4 million to $11.4 million, due primarily to the Hoka brand, which we acquired in September 2012.

At June 30, 2013, our cash and cash equivalents were $49.1 million compared to $114.4 million at June 30, 2012. At June 30, 2013, we had $26 million in outstanding borrowings under our credit facility compared to zero a year ago and $33 million at December 31, 2012.

The decrease in cash and cash equivalents and the increase in outstanding borrowings year-over-year are attributable to $120.7 million of stock repurchases over the past 12 months at an average price of $43.65 a share and $64.5 million of cash payments for capital assets which includes $34.7 million of retail expansion, $17.1 million for the new headquarters facility, and the balance of $12.7 million for IT, infrastructure, and maintenance as well as other expenditures, offset in part by cash provided by operations.

During the quarter we did not repurchase any shares of the Company's common stock and currently have $79 million available under the $200 million stock repurchase program announced in July, 2012.

Now moving on to our outlook. Based on second-quarter results and current visibility, which now includes an increased contribution from our direct-to-consumer channel sales, driven by the opening of approximately 36 retail stores, up from the previous plan of around 30 and stronger e-commerce trends, we now expect revenues for 2013 to increase approximately 8% over 2012 levels compared to our previous expectation of 7%.

For the full year we now expect UGG brand sales to increase by approximately 7% to 8%, up from our previous expectation of 4%. We now expect Teva brand sales to be flat to slightly down compared to our previous expectation of 6% growth and Sanuk brand sales to grow approximately 5% versus our previous expectation of between 10% to 13%. Our other brand sales are expected to generate $39 million of revenues in 2013.

With regard to earnings, we are raising our outlook and now expect diluted earnings per share to increase approximately 8% over 2012, up from our previous guidance of 5%. While second-quarter earnings came in ahead of guidance by approximately $0.25, roughly half of the improved earnings was related to a shift in the timing of certain marketing, selling, and retail and other expenses, which we expect to spend in the second half of 2013. Operating expenses in the back half of the year are also increasing from six additional retail stores we now plan to open plus additional IT investments now scheduled for the fourth quarter.

Our forecast is still based on SG&A as a percentage of sales of approximately 34%. We now expect gross margins to improve an additional 30 basis points above our previous expectation of approximately 46.5%, driven by increased contribution for our direct-to-consumer channel. For the year, capital expenditures are projected to be approximately $85 million to $90 million, with $40 million for retail stores and approximately $40 million for the corporate facility, IT, and other maintenance items. And we are still planning to refinance our corporate headquarters by securing long-term financing.

For the third quarter 2013 we expect revenues to increase approximately 2.5% and diluted earnings per share to decrease approximately 41% over 2012 levels. For the fourth quarter 2013 we expect revenues to increase approximately 14.5% and diluted earnings per share to increase approximately 38%. This quarterly EPS guidance is in line with our previous disclosure and, as a reminder; roughly 85% to 90% of our projected second half earnings are expected to come in the fourth quarter. I will now turn the call back over to Angel.

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

Thanks, Tom. As we take stock of where we are at the halfway point in the year, I am pleased with how the first half has unfolded following a challenging 2012. Obviously there are always areas of the business that we can improve upon and they will control -- there will continue to be factors impacting us that are outside of our control.

That said, I think we're taking the right steps toward affecting positive change at Decker this year and, more importantly, over the long-term. We could not be more confident about our products pipeline that we have in place for fall 2013, just feeding into 2014. I believe fall 2013 is the UGG brand's strongest and most complete line that we've developed.

We've made great progress in one year to broaden the appeal and accessibility of the brand, including having more transitional product to help bridge the gap between late summer and the start of fall weather, to more attractive opening price points in our casual and fashion collections combined with non-core products that better reflect the UGG brand DNA and a broader lineup of specialty classes. And while still very early, sell-through so far in July supports this thesis.

In the US, wholesale inventory levels are much cleaner than they were a year ago and we believe that our retail partners are equally excited about the freshness of the fall line. In Europe we feel like we've turned a corner with the UGG brand in the UK and, with good momentum coming out of Q2 combined with a much stronger product line, we are encouraged about our prospects for growth in the coming holiday season.

We believe that Asia continues to be a source of growth and opportunity, particularly for retail expansion in China and Japan. As we make additional investments to our merchandise offerings and marketing programs based on a better understanding of the regional defenses between East and West, we believe that we can build market share in these two large, important consumer markets.

We look forward to updating you again in about 90 days when we report our third-quarter results. By then we will know a lot more about our sheepskin needs and costs for 2014, which at this point would be premature to comment on. And by late October we will have much better visibility in how the holiday season is shaping up.

Given the unpredictability of whether, especially what has transpired in the last two winters, I think we are taking the right approach to planning the business for the remainder of the year while at the same time investing in new products and new processes that both mitigate our dependence on weather and create new growth vehicles for the future, including the specialty running category where Hoka, our newest brand addition, gives us an immediate and legitimate platform to compete.

With a strong balance sheet and strong cash flow, we are well-positioned to execute on the strategic plans for evolving each of our brands and driving sustainable earnings growth and increased shareholder value well into the future. Operator, we are now ready to take questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Erinn Murphy, Piper Jaffray.

Erinn Murphy - *Piper Jaffray & Company - Analyst*

Great, good afternoon and thank you for taking my question. Angel, I guess my first question is for you. Just you commented earlier on in your script about the direct to consumer business kind of month to date is starting to improve. I am just curious if you could expand upon that comment. You are seeing it more in traffic or is it ticket-based? And what style is the consumer right now gravitating towards?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

Well, we've had actually pretty consistent performance across our entire DTC from the e-commerce business to our own stores -- the Kfar, as I mentioned, consistent styles selling in our wholesale customers as new product has arrived. We've got a little bit of -- we've had success with the sneakers. Once the weather warmed, the sandal started performing.

So in general, and the new fashion product, what we call transitional product, but really it's the right price point in boots and lighter weight early fall product that has been performing well. So -- and we are starting to see the same thing happening as we're getting early reads from our wholesale customers, so we are feeling pretty good about that.

Erinn Murphy - *Piper Jaffray & Company - Analyst*

Okay, that's helpful. And then I guess from a wholesale perspective, and in general kind of across the industry, there's been a lot of concern from both apparel and footwear brands just on the retailers taking a little bit more cautious view in the order book. Can you just articulate on what kind of behavior you are seeing thus far for the fall holiday deliveries?

And then I guess to that, if there's any just update on the backlog. You did comment more orders than inventories. But just any color on both how retailers are feeling thus far this season and then also on your backlog, thank you.

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

I think caution is the right word. I think everyone is approaching, and especially after the last two winters, very cautiously. That's why it's important for us to make sure that we are in a good position to meet their near-term needs with our core product. So we decided to take some product early.

We understand that consumers out there are buying closer to their needs, closer to the season. Retailers are reacting accordingly and we are in a good position to fill in around core styles, which is pretty essential for us assuming of course that we get a more normalized winter. So in general we are feeling pretty good about the inventory position we are in and the availability of the core styles we are filling.

Tom George - *Deckers Outdoor Corporation - CFO*

Erinn, this is Tom. Related to the backlog, there's really no change since the past quarter because, especially for the (technical difficulty) business, it's primarily the wholesale business is primarily pre-booked. But to add some color consistent with the last quarter, the pre-booking came in more skewed to the fourth quarter versus the third quarter because, to some of those points Angel mentioned, the retailers are being more risk-averse early on. They want more products later during their especially peak holiday selling season.

Erinn Murphy - *Piper Jaffray & Company - Analyst*

Okay, and then I guess for the inventory comment as well, it's a better exit in Q2, but could you just talk a little bit about the complexion of this balance between both the independents and the major wholesalers?

Tom George - *Deckers Outdoor Corporation - CFO*

In terms of the inventory in the channel?

Erinn Murphy - *Piper Jaffray & Company - Analyst*

Yes, how are you feeling about the delta between the two?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

I think we feel pretty comfortable there. As time has marched -- we already were comfortable with how our larger wholesale customers, the bigger retailers, how their channel has cleaned up. And I think as time has marched on here, the independents have gotten a little bit cleaner as well, but not to the same level as the larger customers.

Erinn Murphy - *Piper Jaffray & Company - Analyst*

Great. Thank you, guys, and best of luck.

Operator

Sam Poser, Sterne Agee.

Sam Poser - *Sterne, Agee & Leach, Inc. - Analyst*

Thanks for taking my question. I'm going to take your inventory on here. Could you tell us how much inventory -- was it $16 million of inventory that you allowed to come in early? Because you said you would be under $300 million?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

Good question. Let me give you some color on that. We had talked about being at about $300 million; we came in a little over $362 million. At least a little bit of that was related to Teva and Sanuk, a very slight amount. The rest is really mostly timing, and so, you are working with maybe $55 million there and $30 million to $40 million of that $55 million is based on our decision to bring product in early, so we will be better prepared to put the product in our warehouse and service our backlog and our DTC for the back half of the year. And IE not be late on fashion product similar to some of the same things that happened last year.

I think the ad in terms of the quality of the inventory, we gave you some good color about we need to bring more inventory in. Our wholesale order book alone is going to take care of inventory we have at the end of June. So we need to bring more inventory in to be able to service our DTC business as well as have the opportunities to chase some business within --.

Sam Poser - *Sterne, Agee & Leach, Inc. - Analyst*

In all due respect, though, isn't that a -- as you said, that's probably much more of a fourth-quarter story than it is a third-quarter story. So I guess the question for you is what is your target -- given your current sales guidance with the gross margin and everything, what is your target inventory for the end of Q3 and your target inventory for the end of Q4 to set yourself up properly for 2014?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

I think how we would like to communicate on our inventory is we have seen some improvement in it. It's always had great quality and we've never had any large write-off issues. Look at it more on a 12-month moving average kind of basis. And we expect to continue to have our inventory levels more in line with forward sales trends and continued improvement on a 12-month moving average basis over time. And I think we are spending too much focused on the inventory at any one point in time. So I think you need to look at improving trends over time.

Sam Poser - *Sterne, Agee & Leach, Inc. - Analyst*

Yes, but the thing is that the trend because of the business at the end in 2012 -- the end of 2011 through 2012, the inventories were so bloated at that time that you are comparing it off of the higher numbered start with it was too much to begin with. So the year-over-year comparisons don't work anymore. You go back to like Q3 2011 inventories or Q2 2011 inventories to get more of a like for like and so the question is where are your target inventories? I'm thinking you need to be sub $250 million by the end of the year period just to be set up to get your terms right in everything else. Am I in the ballpark and so on?

Tom George - *Deckers Outdoor Corporation - CFO*

I think just a frame of reference to ground everybody in the call, our UGG brand inventory is up slightly, a lot lower than the implied sales growth in the back of the year, which is 10%. So again, you need inventory to be able to service growth in the back half of the year. And we feel good and especially good about the quality of that inventory where we stand and feel pleased with where we are headed on the management of it as well.

Operator

Randy Konik, Jefferies.

Randy Konik - *Jefferies & Company - Analyst*

Quick question. So can you just give us a little bit more color about what the accounts are saying in terms of the -- it sounds like the backlog in the order book is obviously improving. What are they telling you? Are they -- is it because they feel better about the environment? Are they feeling better about the product? The first question is on what specifically are these accounts kind of talking to in terms of impacting the backlog? Thanks.

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

First of all, from a product point of view, great response on the product, so far happy with sell-through on the product. We have actually people who ordered a little light on core classic product; it's starting to worry them. I think they may find themselves in a position to chase some product as the season progresses. Backlog hasn't changed, so we really feel going into this third and fourth quarter pretty confident about the reaction we've had, the response from retailers, the sell-through of the product, the quality of the inventory, all those things are positives.

Randy Konik - *Jefferies & Company - Analyst*

Okay, got it. And then in terms of -- just remind us where we should be at with UGG Pure over the next 12 months.

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

We said it has been -- we're very happy with, by the way, the way in which UGG Pure has evolved. We said the real benefit of UGG Pure will be felt in the more mid to longer-term period. So we had, as you may recall, regular sheepskin that we had to work through in 2013 and we continue to now, as we move through that inventory of raw materials, appropriately replace our needs for table grade with UGG Pure and we are continuing down that path.

Linda Pazin - *Deckers Outdoor Corporation - VP of IR*

And I did have --.

Randy Konik - *Jefferies & Company - Analyst*

Go ahead. Finish your thought and then I have one last question.

Linda Pazin - *Deckers Outdoor Corporation - VP of IR*

No, in regards to UGG Pure we just wanted to remind people that we were also looking at expanding it into our home product and really delivering the best product possible for our consumers with as much diversification as we can. And as Angel mentioned, by the end of 2013 we are looking to deliver up to 10% of our products using exclusively UGG Pure and then up to about 25% in the medium-term.

Randy Konik - *Jefferies & Company - Analyst*

Got it. And then lastly, Tom, just kind of walk us through your thoughts on buyback in the business right now in terms of obviously there's share repurchase activity. How do we think about cash generation in this business over the next 12 months and corresponding buyback activity? Thanks.

Tom George - *Deckers Outdoor Corporation - CFO*

Yes, good question. The business model sets with the margins we have and the investment strategy that generates a lot of good cash flow, good operating cash flow. So we do have that opportunity with that operating cash flow to be able to reinvest in the business. And I think there's more of a lean now to reinvest in the business versus repurchasing stock. That being said, we still have $79 million available on the current authorization and we will -- with that we will be up, we will consider opportunistic repurchase as well.

Operator

As a reminder, please let yourself to one question and one follow-up question at this time. Bob Drbul, Barclays.

Bob Drbul - *Barclays Capital - Analyst*

Good afternoon. I guess, Tom, my question is when you look at your assumptions in the back half of the year in terms of the sales assumptions and the margin assumptions, can you just explain what you would view as conservatism that you have built in? I understand the new stores, but like the margin recovery piece of it and just the sales piece of it, how you've estimated especially the new stores and the retail stores to get to the top-line and the bottom-line assumptions that you are looking for now at this point in time with the visibility that you have?

Tom George - *Deckers Outdoor Corporation - CFO*

We feel comfortable with where we are at on the guidance we put out there for the back half of the year. I think one thing to consider, as we grow our DTC business, we have been seeing improving trends on the e-commerce business. There are some strong trend there and we're getting more and more sort of intelligent and experienced in how to drive more and more business into our e-commerce through our website. So there might be an opportunity there.

On the retail stores, in our guidance we assume we are going to open six more, so i.e. 36 versus the earlier guidance of 30. Obviously as we grow retail around the world, there's always sort of a pool of additional stores, i.e. locations and what not we are looking at, so you have to work with a larger inventory to be able to secure the six additional. So there may be some opportunity there but can't necessarily promise that at this point in time.

We feel good where we are at from a margin point of view and especially the DTC business, where how we can drive additional profit dollars for more DTC money. So if there's -- we end up having more DTC business versus wholesale business in the back half of the year obviously and that could drive a lot of profit opportunity.

Bob Drbul - *Barclays Capital - Analyst*

Great and on the -- the retail business in Japan and in China, I think Japan the 20 and China sequentially improved and is still negative. Can you just elaborate a little bit more on both of those markets and sort of the game plan especially in China going forward?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

Japan, really pleased with that. For the quarter I think every store comped positively. If you go over to that market and just see the energy in the market you can just see how our product is really -- the changes we've made to the product offering there and how we are driving traffic to the stores, you get pretty excited. And in some of the new stores we're opening and some of the locations are very high-traffic locations with the right demographics, so very excited about Japan.

And China is getting the better inventory fill, broader product assortment, some product learning, some more marketing around awareness of the brand and driving traffic to the stores in China. It's what makes us excited about that opportunity, what has helped drive the improvement there.

Bob Drbul - *Barclays Capital - Analyst*

Great. Linda, congratulations. Good luck.

Operator

Taposh Bari, Goldman Sachs.

Taposh Bari - *Goldman Sachs - Analyst*

Good afternoon. I wanted to ask a question about UGG wholesale in the second quarter. My math gets me to UGG wholesale being down about 20% in the quarter. Is that right? And if so, it looks like you are modeling a more stable growth rate year-over-year in the back half just kind of backing into the numbers. So A, just curious to know what drove the decline in the second quarter I guess to start.

Tom George - *Deckers Outdoor Corporation - CFO*

From a modeling point of view, in the second quarter you're pretty close to where we ended up in the second quarter for UGG. It was a combination of not only the domestic business but some of the international business as well. And going forward we still have -- that's pre-booked, so in the back half we have cautious expectations as well for our wholesale business in the back half.

Taposh Bari - *Goldman Sachs - Analyst*

Okay, and I guess on that point, I think historically your business has been largely pre-booked for the fall/winter business. Does the composition -- I know the retailers are buying closer to need and receiving closer to need, but does the composition for the entire season change of pre-book versus at once this year versus last?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

No, not really other than -- with two tough winters where we had a fair amount of cancellations, we still maintained some cautiousness around cancellations and very little reorders in our projections.

Taposh Bari - *Goldman Sachs - Analyst*

Okay, that was my other question -- for reorders are you assuming kind of flat reorders, reorders to be up, down, if you can give us any kind of context there?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

Virtually none.

Taposh Bari - *Goldman Sachs - Analyst*

Virtually none? Hopefully it's better than that. Right? Last one for you, Tom. Last one for you is square footage. I think you've been providing that for the past couple of quarters, square footage in the last 12 months, sales per square foot. Are you no longer providing that or --?

Tom George - *Deckers Outdoor Corporation - CFO*

I think we did. We provided the square footage in there. It was -- sales per square foot on an annualized basis with a comp basis around $1,500 and total square footage as well over 200,000 square feet now.

Taposh Bari - *Goldman Sachs - Analyst*

Okay, thanks a lot. Good luck.

Operator

Omar Saad, ISI Group.

Omar Saad - *ISI Group - Analyst*

Thanks, guys. Can you -- so you guys have guided to the second quarter kind of top-line last quarter around flat, and I know this is the smallest quarter, but came in a little bit below that. But you raised the revenue guidance for the full year. Can you just tell me understand what are the areas of the business that give you the confidence despite a little bit softer Q2 top-line.

Maybe you would had anticipated that you kind of felt like it was appropriate to bring up the full year? Are there certain things going on with some of the brands, certain categories, is it the DTC side of it, it sounds like the Internet business is strengthening? Any insight there would be helpful and then I have one follow-up.

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

It's the DTC business. We feel more and more comfortable with that. We have had improved e-commerce trends and we're going to open -- and the guidance assumes we open six more stores than we did before. So that gives us the comfort level on the revenues. I think that ripples through and gives you more margin dollars to work with as well and there's some additional OpEx to offset that. But that gets you to a revised guidance that gets our earnings growth in line with our sales growth as well. So that's why we -- that's the driver of the improved guidance.

Omar Saad - *ISI Group - Analyst*

Understood, thanks. And then, Angel, could you talk about a little bit as you're getting a little more opportunity to work with the UGG Pure material and integrate it into some of your products and think about it going forward. Can you talk about the design teams and the designers in the Company? There are some interesting ideas about being able to do more with the product from a design standpoint with those materials from a design standpoint? Are we going to see -- have an opportunity to see comes from new styles with the UGG pure this fall? And rolling out next year, just any update on that front would be really helpful.

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

You're going to see -- I think probably the operative word for the design team when it comes to UGG Pure is liberating. Because really what it does is it allows for even color; for example, there are limitations in what you can do in color with conventional sheepskin because of -- certain colors it doesn't take well. They are too caustic on the skin side of the hide. UGG Pure allows us a lot more diversity in color, which is really important.

From a texture point of view, we have the opportunity to engineer different textures into the material which we never had that opportunity before. Overall, sort of the pile itself, in other words the density of the material we can vary that. So it allows us to make product that is less bulky and as a result allows us to have your more form fitting footwear.

Which one of the things we found out from consumers who were objecting -- they were interested in the brand, they love the slippers but they were objecting to the shoes as outdoor fashion because the product was too bulky. Now this allows us to have much more closer to the foot shapes and feel for the products.

So those are all things that are liberating to the design team and you will see over the next several quarters' tremendous innovation when it comes to the product design. I think fall 2014 is something I've already previewed, obviously. Now that is just very exciting product. I have never seen anything like that from our brand and that's only possible because of what UGG Pure has allowed the designers to now think about and go execute.

Omar Saad - *ISI Group - Analyst*

Understood. And will some of that be at the fall shows this year, the preview lines?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

Yes, you will see -- fall 2014. You will see that in the preview lines and we'll have our (inaudible) show will have a product preview at our showroom.

Omar Saad - *ISI Group - Analyst*

Great. Thanks, guys.

Operator

Corinna Freedman, Wedbush Securities.

Corinna Freedman - *Wedbush Securities - Analyst*

Just a quick question on -- you mentioned slippers are now a year-round category. Are there any opportunities to pick up pricing there or to expand that line any further?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

We have this year introduced an $80 price point in slippers again because of some advantages we have with UGG Pure. It allowed us to actually make a slipper that for warmer climates is not quite as bulky. It's been very successful, very popular. Our continued success of our men's Ascot continues to develop around the world.

We are building a slipper business in markets outside the US where really in the UK, for example, they had not really seen a slipper business, so we are pioneering an entire category of footwear in the UK. So you are going to see a lot more diversity again of color, of style, of the density of the material to allow us to evolve that business where we are the market leader by a long stretch there.

Corinna Freedman - *Wedbush Securities - Analyst*

Okay, and then my second question is have you changed your philosophy about expanding distribution any for this year given your inventory? And just maybe there was some weakness I think in the higher end department stores and would you consider opening up some mid-tier department stores? Just if you have any updated thinking about that.

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

We are very comfortable with our wholesale distribution. We have been cleaning up our distribution here and there in various parts of the country where we felt in some cases we were not being well represented. That's an ongoing process. We have evolved to a very sophisticated direct-to-consumer model with our outlet stores and concept stores in the mix and that certainly negates the need to run out and open less than desirable distribution in our mind. We feel we have excellent wholesale partners across all channels and we don't see a need to go beyond that in the near term.

Corinna Freedman - *Wedbush Securities - Analyst*

Okay, great. Thank you. Good luck.

Operator

Mitch Kummetz, Robert Baird.

Mitch Kummetz - *Robert W. Baird & Co. - Analyst*

Thank you. I want to begin -- I just want to go through some of the assumptions. There are some assumptions that were discussed on your Q1 earnings call. I just want to be clear that we are still looking at kind of the same assumptions. So on your own stores I think it was mentioned last call you are looking for a flat comp. And I just want to be clear that that's still the case in the back half or do you now expect it to be better than that given some of the trends that you are seeing at retail -- or within your own stores?

Tom George - *Deckers Outdoor Corporation - CFO*

Mitch, this is Tom. We talked about it -- the last call I think we talked about a flat to slightly up comp for the total year. For the total year that's similar to what we were looking at now, flat to low single-digits kind of comp for the total year.

Mitch Kummetz - *Robert W. Baird & Co. - Analyst*

Okay, that's helpful. And then I think you had also said last time that you thought UGG wholesale would be down sort of mid to high single-digits for the year kind of based on the way your order book was shaping up and kind of your assumptions on cancellations and reorders. Is that still the case then as well?

Tom George - *Deckers Outdoor Corporation - CFO*

Yes, it's more for the total -- sort of the first half of the year is behind us. Looking towards the back half right now is probably what you're more focused on. When you look at in our guidance for the back half of the year, the UGG domestic wholesale business is down more like a mid -- down mid single-digits kind of.

Mitch Kummetz - *Robert W. Baird & Co. - Analyst*

Okay, and then I know, Tom, you said that you are not assuming any material -- or on the reorder side, really any material improvement there. Actually I think you said you are really not looking for any reorders. I think last call you said you were expecting a similar level of cancellations as well as last year. Is that still the case then?

Tom George - *Deckers Outdoor Corporation - CFO*

Yes, on the cancellation side, that still is the case.

Mitch Kummetz - *Robert W. Baird & Co. - Analyst*

Okay, then real quick on Pure, I'm just trying to still get a better handle as to what the cost-benefit is on that. And let me ask the question this way. If you look at like a foot bed or a lining and you compare Pure to, like, table grade sheepskin, how much of a cost differential is there going from like table grade sheepskin on a foot bed or a lining to Pure in those components? Is there anyway you can give me a sense of that?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

This is Angel. First of all, it's significantly better from a cost point of view. They haven't been specific in how much per square foot, etc., but more important than that it's better product. The UGG Pure footbed doesn't compress and doesn't sort of develop bare spots. It's just more durable and that's from our experience.

We will continue to evolve that technology, continue to develop the testing procedures as we continue to evolve the product, but from our reviews so far, it's just better product. And the consumer will vote accordingly, but I think they will be presently surprised.

Mitch Kummetz - *Robert W. Baird & Co. - Analyst*

All right, thanks. Good luck.

Operator

Scott Krasik, BB&T.

Scott Krasik - *BB&T Capital Markets - Analyst*

Thanks, given the new store openings abroad and the momentum in Japan, can you just update us, Tom, sort of the size of the markets ranking behind the UK? Is Benelux still the number two market? How do they compare to China and Japan now?

Tom George - *Deckers Outdoor Corporation - CFO*

Let me -- I've got that handy. For the total year and let me give you a frame of reference. I'll give you last year's reference. The UK was our biggest international market and then Japan actually was number two. Benelux number three and China number four. This year the UK is still the largest market, then Japan comes in number two, China three and Benelux number four.

Scott Krasik - *BB&T Capital Markets - Analyst*

Okay, that's awesome. And then are the issues affecting China and Benelux similar and are the solutions similar or how do you frame the issues there?

Tom George - *Deckers Outdoor Corporation - CFO*

Different things. Benelux it's really a wholesale business, a lot of macro issues there. To the point that the consumers when they do buy any brand's product they down select to the most affordable so that's putting ASP pressure. Still some distribution issues there similar to what we had in the UK before we changed that around, so we need to work on that.

China, that's a retail market. We opened a lot of stores. We are good at opening stores. We now are adding the infrastructure and the personnel and the executive experience to be able to operate stores at a better rate and work on comps and make sure we have the inventory and make sure we merchandise the stores correctly and those kinds of things, so that's why we are starting to see some improvements on the China comps.

Scott Krasik - *BB&T Capital Markets - Analyst*

Okay, Tom, that's really helpful. And then just last -- when we were in Nordstrom's, the Nordstrom's last weekend, the store associates kept saying it's a no-brainer for the Roni at $89.90 or the Alloway. Where are you in terms of introducing product at price point? Will we see even more next year?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

Yes, you will definitely see more. Really this is going to become a power alley for the brand. It's one of the things that we are very excited about and again given the flexibility that we have with raw materials, it allows us to address price points that we had to abandon because of the rise in sheepskin pricing over the last five years or so. So we are very excited about not only the price points, but really the fashion, the quality, everything that we are seeing in the fall 2014 line. I'm very excited to show you all what that looks like. It's going to be a breakthrough and you'll see for yourselves.

Linda Pazin - *Deckers Outdoor Corporation - VP of IR*

And then I also just wanted to add with Nordstrom's that we are really pleased with the results we are seeing in the offering, which is more transitional, more fashion product, which is buy now/wear now. And consumers are really responding to getting more of that transitional product.

Scott Krasik - *BB&T Capital Markets - Analyst*

Yes, we definitely saw that. Thanks, guys, and good luck.

Operator

Camilo Lyon, Canaccord Genuity.

Camilo Lyon - *Canaccord Genuity - Analyst*

Thanks, guys. I just wanted to go back to the inventory issue for one minute. Could you just help me understand where does the confidence level come from to take on more inventory and hold that in your DC if the retailers aren't necessarily committing to taking that product earlier? I know you guys are nice guys, but that seems to not jive totally with what we are hearing from retailers and how they are trying to position their business.

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

Just to confirm what we talked about earlier, Camilo, we actually have more orders than we have current inventory levels right now. So we need more inventory to service the current orders. So that's obviously a good position to be in from that point of view. And I think another thing to give everybody -- just to remind everybody the frame of reference in terms of how the Company is transforming into more DTC business versus wholesale and distributor kind of business.

You need inventory to support the DTC business, obviously both the e-commerce in the retail stores. And you need more drops of inventory over the course of the year and during the season, have more and more fresher products. So as a result of that, you need to have more inventory. One other point, I don't want to -- I can't say it really enough. We don't have -- with the strength of the brand we don't have any issues from a major inventory write-off that maybe some other brands would have.

And another thing to point out, we did have some closeouts like any other footwear brand in the first quarter, but nothing really of any significance. In fact by the time it gets ready to finalize our closeouts for the quarter, sometimes I wish we could find more product to closeouts. So we've got a brand -- back to the strength of the brand -- it's been around for 35 years. So we've got some experience in terms of how to manage inventories as well.

Camilo Lyon - *Canaccord Genuity - Analyst*

Okay, and so the incremental $30 million to $40 million of inventory that you talked about, if the UGG inventory is only up decimal points, is that inventory then fashion-related product?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

It's accommodation of both, the transitional product for the third quarter as well as some additional what we call heritage kind of product as well as other casuals and it's a broad spectrum of a lot of different -- lots of different product. We would rather get our hands on that inventory to be able to have it in our warehouse because we have -- move a lot of inventory through our warehouse during the peak selling season.

We don't have to sit there and worry about waiting for inventory to be on the water. And this also enables the supply chain, especially our factories, to have more capacity to be able to manufacture even more product to meet the current order book we have because, again, right now our order book is higher than the current inventory we have on hand.

Camilo Lyon - *Canaccord Genuity - Analyst*

So if you had more inventory, then one would be led to believe that your revenue guidance would be higher. Is that correct?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

Well, I think let's look at this. Currently our UGG inventory at the end of June is up 2.5%, 3%, mid single-digits. Our implies guidance for the back half of the year of UGG sales growth is up double digits, a 10% kind of number. So we are going to need more inventory to drive that kind of growth and we will also have inventory available in the key styles to chase some business into (inaudible).

Camilo Lyon - *Canaccord Genuity - Analyst*

And then just lastly on that, so do we expect the Q3 inventory to be lower by $30 million to $40 million or will it be higher than $30 million to $40 million, of that increment that you took on sooner?

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

I think how we want to get everybody to view our inventory is continued improvement over time, which we've demonstrated on a year-over-year basis. And the inventory is more in line with forward sales guidance and the quality will continue to be very strong.

Operator

Howard Tubin, RBC Capital Markets.

Howard Tubin - *RBC Capital Markets - Analyst*

Thanks, just maybe one question on average pricing. Maybe given all the initiatives you are working on in UGG Pure, what is kind of the average UGG price going to look like -- or maybe pricing on the collection this fall versus last fall? Maybe 2014 versus 2013 is going to be trickling down over time.

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

I think is a continue to develop transitional product, the transitional product is at a lower average selling price. That said, as I mentioned in my comments, we are moving more units, so we are putting more people in the brand, which is a very positive thing. When it comes to the high selling season, the core assortments, that remains at the traditional price points. And as we have experienced over the last few years, we have been able to mitigate taking a radical price increase. So we expect stability there in the core assortment.

So really you sort of have to look at our business as from two perspectives. One is what's happening with price points in the peak season of core product selling, those price points will remain where they've been. And then we are introducing new product, new consumers into the brand, and lower average selling price. So if you take the net-net of it all, we probably over time will see as our business in the second and third quarter grows with transitional product, you're going to see the average selling price come down a little bit and then bounce back up in the fourth quarter with the core certain.

Howard Tubin - *RBC Capital Markets - Analyst*

Got it. Okay, thanks.

Angel Martinez - *Deckers Outdoor Corporation - Chairman, President & CEO*

Thank you all very much for participating on the call. We look forward to updating you in 90 days as we move toward a successful conclusion of 2013. Thanks a lot.

Operator

That does conclude today's program. Thank you all for joining today.
