Corrected Transcript

24-Oct-2013

Columbia Sportswear Co. (COLM)

Q3 2013 Earnings Call

CORPORATE PARTICIPANTS

Ron Parham
Senior Director-Investor Relations, Columbia Sportswear Co.

Gertrude Boyle
Chairman, Columbia Sportswear Co.

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.

OTHER PARTICIPANTS

Lindsay Drucker Mann
Analyst, Goldman Sachs & Co.

Katharine McShane
Analyst, Citigroup Global Markets Inc. (Broker)

Laurent Vasilescu
Analyst, Macquarie Capital (USA), Inc.

Corbin Nicholas Weyer
Analyst, Robert W. Baird & Co. Equity Capital Markets

MANAGEMENT DISCUSSION SECTION

Operator: Greetings. And welcome to the Columbia Sportswear Third Quarter 2013 Financial Results Conference Call. At this time all participants are in listen-only mode. A brief question and answer session will follow the formal presentation. [Operator Instructions] As a reminder this conference is being recorded. It is now my pleasure to introduce your host, Ron Parham, Senior Director of Investor Relations and Corporate Communications with Columbia Sportswear. Thank you, Mr. Parham. You may begin.

Ron Parham
Senior Director-Investor Relations, Columbia Sportswear Co.

Thanks, Bob. Good afternoon and thanks for joining us. Earlier this afternoon we issued a press release announcing third quarter financial results and raising our full-year 2013 operating income outlook. In keeping with our standard practice, we also furnished an 8-K and posted to our Investor Relations website a detailed commentary by Chief Financial Officer, Tom Cusick, analyzing third quarter results and our revised outlook. We hope you've taken the opportunity to review the CFO commentary prior to this conference call.

With me today on the call are our President and CEO Tim Boyle; Senior Vice President and Chief Financial Officer Tom Cusick; Executive Vice President and Chief Operating Officer Bryan Timm; and Senior Vice President and General Counsel Peter Bragdon.

I'll ask Chairman, Gert Boyle to cover the Safe Harbor language.

Gertrude Boyle
Chairman, Columbia Sportswear Co.

Good afternoon. This conference call will contain forward-looking statements regarding Columbia's business opportunities and anticipated results of operations. Please bear in mind that forward-looking information is subject to the many risks and uncertainties, and actual results may differ materially from what's projected. Many of these risks and uncertainties are described in Columbia's Annual Report on Form 10-K for the year ending December 31, 2012, and subsequent filing with the SEC.

Forward-looking statements in this conference call are based on our current expectations and beliefs, and we do not undertake any duty to update any of the forward-looking statements after the date of this conference call to conform the forward-looking statements to actual results or the change in our expectations.

Ron Parham

Senior Director-Investor Relations, Columbia Sportswear Co.

Thank you, Gert. I'll turn the call over to Tim.

Timothy P. Boyle

President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.

Thanks, Ron. Welcome, everybody, and thanks for joining us this afternoon. As detailed in our press release and CFO commentary, third quarter sales and profits exceeded our July outlook, primarily due to better-than-expected sales and margins from our U.S. direct-to-consumer and wholesale channels combined with continued focus on controlling SG&A spending. Inventory at September 30 was down $66 million or 14% from last year at this time, the second consecutive quarter of double-digit improvement, following a 19% reduction at June 30. We also raised our operating income outlook for the full-year by approximately 8% compared with our July outlook, based on results through the first nine months and the continued strength we have seen in our U.S. direct-to-consumer and wholesale channels in the early weeks of Q4.

Although there have been plenty of reports recently about the generally soft U.S. retail environment, all three formats of our U.S. direct-to-consumer platform, branded stores, outlet stores, and e-commerce produced better-than-expected results during the third quarter and we've seen that continue into October. The most encouraging aspects of our direct-to-consumer business is the strength we're seeing in our branded stores and e-commerce. Both formats saw stronger conversion and higher average dollars per transaction. We're seeing strength across all categories and genders with many of our pinnacle fresh styles performing well. The Sorel brand is also performing well in our retail stores at selected wholesale customers and particularly on our e-commerce site.

In addition to strong sales of our established styles, our new fall items have also sold well suggesting that Sorel has a bright future beyond winter with fashion forward female consumers as they become more aware of the brand's broader offering. Sorel's fall 2014 product line will offer more back-to-university designs and our sales force will be working closely with our wholesale customers to place larger, broader assortments so that more consumers can discover them at retail next year.

Turning to our EMEA region, third quarter net sales grew $17.6 million or 29%. This increase was entirely attributable to a timing shift in fall 2013 shipments to our EMEA distributors, more than offsetting a mid-teen percentage decline in our Europe direct markets. We believe our business in key European direct markets is stabilizing as we've met or slightly exceeded our internal wholesale forecasts in each of the past few months. We're focused on returning to sales growth in that region in 2014.

As we announced in September, we're looking forward to welcoming Franco Fogliato as our new Senior Vice President of Europe effective November 4. Franco brings 17 years of European sales and marketing experience in the action sports and outdoor footwear and apparel industries having served since 2004 as General Manager of Europe and a member of the executive board of Billabong where he managed the company's portfolio of eight brands. From 1997 through 2003 Franco held various European leadership roles with The North Face brand, culminating as General Manager of Western Europe. Franco understands the European consumer and has strong relationships with our valued wholesale customers throughout the region. Europe remains a critical region for our company's long-term success. We look forward to Franco's contributions as we seek to drive consumer demand and renewed growth in these markets and to improve the region's profitability.

Looking now towards the LAAP region. Third quarter net sales declined 15%, including a 9% negative effect of changes in currency exchange rates. Our businesses in this region are performing well with the exception of Argentina and Venezuela and Australia. Venezuela and Argentina have historically been significant markets within our LAAP region. However, this year sales to our Argentinean distributor have been severely hampered by government trade restrictions. In addition, currency controls in Venezuela have stifled our sales into that market. Both of these situations are purely political in origin. Our brands are strong in this region. However, there is no indication of when these political issues might be resolved.

In Australia and New Zealand the transition to a new distributor caused a temporary sales decline. However, our new distributor is ramping up its operations and we expect them to establish a healthy business for our brands in those key markets. Our Japan and Korea subsidiaries continue to post healthy growth on a local currency basis, although the weaker yen caused Japan's reported sales to show a decline.

Also within the LAAP region we are making final preparations to commence a new joint venture in China on January 1, 2014 with our current distributors Swire Resources Limited. We expect this joint venture to contribute meaningfully to 2014 sales and earnings growth, and we will have more to share on that subject on our February 18 call when we plan to announce our fourth quarter and full-year 2013 results along with our preliminary financial outlook for 2014.

Finally in Canada, third quarter sales fell a bit short of our plan because some shipments moved from the third quarter into October as we transitioned into a new warehouse management system in our Canadian distribution center.

Before we open the call for your questions, I want to reiterate our continued progress on inventory management and discretionary spending. The 14%, $66 million decline in inventory is primarily due to an improved flow of fall inventory and in response to a cautious approach by our North American and European wholesale customers in placing advance orders for winter products. The decline also reflects many enhanced processes across our planning and supply chain operations that were implemented to improve inventory utilization and enable us to operate on less inventory relative to sales.

One goal of those new processes is to more closely match the flow of our inventory receipts with customers' requested delivery dates, especially during our large fall shipping season. The fact that we improved our order assignment metrics during our larger shipping season suggests that these new processes are having the desired effect and making us a more reliable vendor for our customers.

Continually improving inventory turns and gross margins remain key priorities for us. We expect consolidated inventory levels at December 31 to be lower than last December, including the approximate $25 million of incremental inventory attributable to the new China joint venture.

We are prioritizing spending towards the key initiatives that we believe will drive future growth and profitability, including the expansion of our direct-to-consumer platform, the launch of our China joint venture in January of 2014, and our U.S. ERP implementation which continues to be targeted for April of 2014.

While I am pleased with the team's ability to manage inventory and costs, we are far more focused on reigniting sales growth in each of our brands and geographies. We structured our fall 2014 product lines to offer a greater percentage of high performance styles at more accessible prices to drive volume and profitable growth for us and for our retail partners.

As we look ahead to 2014, we see several factors that we expect to drive renewed sales and earnings growth: improved product assortments that are better positioned and segmented across channels to drive volume and profitable growth; Initial reactions from our global wholesale customers to our 2014 product lines are very positive; Incremental sales and earnings from the new China joint venture; continued growth and expansion of our global direct-to-consumer platform. We see signs of stabilization and a potential return to growth in North America and European wholesale markets.

Our improved business processes will allow us to develop innovative products more efficiently, operate at less inventory relative to sales, and develop stronger partnerships with our wholesale customers and focus on prioritizing and efficiently managing spending.

The combination of these and other encouraging factors led us to propose and our board to authorize a 14% increase in the company's quarterly cash dividend, raising it to $0.25 per share from the prior rate of $0.22.

If you have not already done so, I strongly encourage you to read the CFO commentary which we furnished to the SEC on Form 8-K earlier this afternoon and also posted on our Investor Relations website at columbia.com/investor. In addition to the discussion of our Q3 results and the updated outlook, I want to direct your attention to the section beginning at the top of page eight which explains changes we plan to make to our financial outlook protocol in 2014.

That concludes my prepared remarks. Let's open the call to questions. Operator, can you please help us out?

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instruction] Our first question comes from the line of Lindsay Drucker Mann with Goldman Sachs. Please proceed with your question.

Lindsay Drucker Mann
Analyst, Goldman Sachs & Co.
Q

Hi, good afternoon, everyone.

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.
A

Hi, Lindsay.

Lindsay Drucker Mann
Analyst, Goldman Sachs & Co.
Q

I was hoping you could give a little more detail on the U.S., specifically on the wholesale side I know that some shipment timing issues were something that you talked about. Do you have specifics on how much that impacted your results this quarter?

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.

A

Certainly, well as we said earlier, our customers were very cautious in approaching their initial buys for fall 2014. So, we think that the channel is quite clean right now. There's plenty of inventory obviously there, but we expect that with any kind of weather we're going to have a fairly significant growth in our business in the fall in the back half of the year. So, is that the kind of a detail you're looking for?

Lindsay Drucker Mann
Analyst, Goldman Sachs & Co.

Q

Did you have any negative impact on the revenue you booked in the third quarter based on wholesalers delaying orders out of third into fourth quarter?

A

No. I would say Lindsay, actually, our U.S. wholesale business exceeded our internal forecast and was a major component of our revenue beat in Q3, and we're seeing less shift from Q3 to Q4 than we anticipated back in July.

Lindsay Drucker Mann
Analyst, Goldman Sachs & Co.

Q

Okay. And then what did your store's comp, can you tell us the comp figure?

A

Our retail business performed in the U.S exceptionally well, but we don't publish comp store or same-store sales figures.

Lindsay Drucker Mann
Analyst, Goldman Sachs & Co.

Q

Did you see an acceleration in comp versus the second quarter sequentially?

A

Yes, we did.

Lindsay Drucker Mann
Analyst, Goldman Sachs & Co.

Q

So I guess what I'm trying to get at is we've seen an overall softer consumer environment. You haven't had necessarily great weather, so what are you attributing the incremental strength to?

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.

A

Well, frankly I think our products our under distributed in the market. We've got high demand in our own direct-to-consumer operations, and that's because I think consumers are looking for our brand and they are not necessarily able to find it everywhere they'd like.

Lindsay Drucker Mann
Analyst, Goldman Sachs & Co.
Q

Okay. And then so how do we think about incremental margins on the new sales that come in?

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.
A

Well, as we said, our lift is not expected to be on the top line; it's more expected to be on margin, and we have a certain amount of merchandise model to be sold at off price. Whether it dictates a higher demands for those products, we'll have a higher gross margin on whatever we sell through the balance of the year.

A

And Lindsay I think you'll see that reflected in our updated outlook for the rest of the year given we took that gross margin outlook I think close to 50 basis points of which we're up over 30 basis points year-to-date.

Lindsay Drucker Mann
Analyst, Goldman Sachs & Co.
Q

Great. Thank you everyone.

Operator: Thank you. Our next question comes from the line of Kate McShane with Citi. Please proceed with your question.

Katharine McShane
Analyst, Citigroup Global Markets Inc. (Broker)
Q

Hi, thanks. Good afternoon.

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.
A

Hi, Kate.

A

Hi, Kate.

Katharine McShane
Analyst, Citigroup Global Markets Inc. (Broker)
Q

I had two questions. The first question is following up on the previous question. Do you think there was a similar level of sell through at your wholesale partners similar to what you saw in your DTC business? And if not, how can you reconcile that?

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.
A

Certainly, yes, I think our sell-through at our wholesale partners was maybe not as extensive as the sell-throughs we've seen in our stores, and I really don't know how to particularly rectify that other than say there's competitive merchandise in those other stores, in our wholesale partner stores, and we don't have those kind of competitive products in our stores obviously.

Katharine McShane
Analyst, Citigroup Global Markets Inc. (Broker)

Q

Okay. And I know your new head of Europe is not even there yet, but do you expect to alter your strategy meaningfully in Europe now that things have stabilized a little bit, and on your wish list what do you think is the first thing that really needs to be addressed as you try to improve this business going forward?

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.

A

Certainly. Well Franco has not yet started, but we're anxious for him to do so, but in the last really 18 months I've spent a tremendous amount of time in Europe myself working directly with customers, and it's been an easy conclusion that the product missteps that we've had in the U.S. were also similarly – were similarly impacting our business in Europe. We moved to a higher position in the marketplace too quickly and abandoned basically the company's traditional brand positioning. So I've had an opportunity to show our customers in Europe, the major customers in Europe our plans for fall 2014. They have been embraced. So my expectation is that as we roll out these new products in the U.S. and in Europe, our business should improve. So we're not expecting any kind of a major change in the market. If there is anything it's perhaps more focus on a smaller number of markets than we've been attacking in the past, but strategically we're going to be approaching it with the same kind of rigor and focus on the right brand positioning that we have here in the U.S.

Ron Parham
Senior Director-Investor Relations, Columbia Sportswear Co.

A

Operator?

Operator: Thank you. [Operator Instructions] Our next question comes from the line of Laurent Vasilescu with Macquarie. Please proceed with your question.

Laurent Vasilescu
Analyst, Macquarie Capital (USA), Inc.

Q

Hi, good afternoon. This is Laurent in for Liz. I know you no longer give backlog, but do you have any – enough visibility right now to give indication that 2014 will return to growth?

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.

A

Well, I'll say we aren't giving backlog guidance and just to remind everybody that's because there are so many factors now in the business, including our own – the impact of our own direct-to-consumer business, it just was becoming a highly complex exercise to keep everybody focused on what it is we – how it is we looked at the business. But we've certainly seen enough activity as it relates to orders and we know enough about what our customers are purchasing from us versus others to expect that we will in fact have some growth in 2014. I also want to remind you that China is a big part of our future and that business will be significant to helping us on a global basis get bigger in 2014, but we're very excited and frankly our board wouldn't have authorized a further enlargement of our dividend had they not seen these kinds of opportunities and been convinced of them.

Laurent Vasilescu
Analyst, Macquarie Capital (USA), Inc.
Q

Okay, great, thank you. And also can you provide more color on your goals for China with the Swire JV, does the China JV of $25 million in inventory suggest the region can do a multiple of that in the first year?

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.
A

Yeah, the $25 million is just the inventory that the JV will acquire January 1 or December 31 in fact as part of the go live. That business did in excess of $150 million in revenue in 2012 and has grown historically at double-digit rates.

Laurent Vasilescu
Analyst, Macquarie Capital (USA), Inc.
Q

Okay, great, thank you. And then lastly, I'm curious to know if you have a long-term goal for your direct business as a percentage of revenues longer term?

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.
A

Well, I want to remind everyone that our business really is first and foremost a wholesale business, that's our primary focus and how we built the infrastructure to provide support to retailers. And so, our expectation is that selling our products through third-party retailers will continue to be the dominant portion of our business. So, we don't have a plan for retail to grow significantly beyond that.

Laurent Vasilescu
Analyst, Macquarie Capital (USA), Inc.
Q

Okay. Thank you very much. Best of luck.

Operator: Thank you. Our next question comes from the line of Corbin Weyer with Robert W. Baird. Please proceed with your question.

Corbin Nicholas Weyer
Analyst, Robert W. Baird & Co. Equity Capital Markets
Q

Yeah, good afternoon. Thanks for taking my question. Tim, you touched upon a bit that if weather plays during the fourth quarter here, we'd see gross margin versus top line being the bigger beneficiary. Could you just may be talk about what kind of weather assumption are baked into the fourth quarter guidance laid out today. Now are you assuming similar weather to what we saw the past two years or normalized weather, any commentary around that will be very helpful?

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.
A

Certainly, no. I'm happy to do it. So, we've taken normal weather, so that would include some cold to be starting to accumulate. Now we've seen I think the last – this week was called colder than normal in most parts of the United States. We've already had fairly significant cold weather in Russia, which has impacted our sell-throughs there positively. But today we're just planning on normal weather and as you noticed by the emphasis on our inventory reductions, we have not taken a highly speculative position on inventories. So, we feel we're in a terrific position regardless of the weather.

Corbin Nicholas Weyer
Analyst, Robert W. Baird & Co. Equity Capital Markets

Q

That's helpful. Thanks a lot guys. Good luck.

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.

A

Thanks.

A

Thank you.

Operator: [Operator Instruction] There appear to be no further questions at this time. I'd like to turn the call back over to management for closing comments.

Timothy P. Boyle
President, CEO, Director & Executive VP-Global Sal, Columbia Sportswear Co.

All right, thank you everyone for listening in. We're looking forward to a great cold weather surprising us all. Thank you very much.

Operator: This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.