

# FINAL TRANSCRIPT

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## VFC - Q2 2010 VF Corporation Earnings Conference Call

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**Bob Shearer**

*VF Corporation - CFO*

**Jean Fontana**

*ICR - SVP*

**Carl Heinz Salzburger**

*VF Corporation - VP of CF International*

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**Jim Duffy**

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## PRESENTATION

**Operator**



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Good day and welcome to the VF Corporation second quarter 2010 conference call. Please be aware that today's conference is being recorded. At this time, I would like to turn the conference over to Jean Fontana with ICR. Please go ahead.

**Jean Fontana** - ICR - SVP

Thank you. Good morning, everyone. Thank you in participating in VF Corporation's second quarter 2010 conference call. By now you should have received today's earnings press release. If you have not, please call (203)682-8200 and we will send you a copy immediately following the call. Hosting the call today is Eric Wiseman, Chairman and CEO of VF.

Before we begin, I will like to remind participants, certain statements included in today's remarks and the Q&A session may constitute forward-looking statements within the meaning of the of the Federal Securities laws. Forward-looking statements are not guarantees, and actual results may differ materially from those expressed or implied in the forward-looking statements. Important factors that could cause actual results, collaborations or financial conditions of the Company to differ are discussed in the documents filed with the Company and the SEC. I would now like to turn the call over to Eric Wiseman.

**Eric Wiseman** - VF Corporation - Chairman, CEO

Thanks for joining us today. Thanks, Jean. Good morning, everyone and thanks for joining us today. Following my opening comments, Bob Shearer is going to review the quarter's results in more detail. We also have with us by phone today Karl Heinz Salzburger, President of our international business, who is going to provide a recap of our results in Europe and Asia. It's obviously very gratifying to be here today talking about a 47% increase in earnings per share, particularly following a first quarter where earnings rose 60%. It's been an amazing first half for VF, delivered by a very talented global team that's focused on winning in any environment. While we did not provide revenue or earnings guidance for the second quarter, it's clear our results again surpassed both our and the street's expectations. The good news is that the upside was broad based, with better than expected results across nearly all our businesses. Not only were revenues stronger than we anticipated, but similar to what we've seen in the last couple of quarters, our gross margins expanded significantly, which in turn help drive earnings per share to an all time record high.

Taking a quick snapshot of the quarter, compared with last year, every coalition posted higher revenues and operating income, and nearly every coalition posted higher operating margins. We are especially pleased by the return to growth in our jeanswear and image wear businesses. We recognize that these comparisons are against what was a very weak quarter last year, but I think it's clear to everyone that there's been some deceleration at retail since the first quarter. And yet, our top line continued to gather momentum. Based on very strong first half results, we're pleased to announce today increases in our four-year guidance for both revenues and earnings per share. We've raised our target for top line growth by 100 basis points to 4% to 5% growth from 3% to 4% growth. Earnings per share are now expected to increase 18% to \$6.10 versus our prior guidance of \$5.90. As noted in the release, this includes a greater negative impact to foreign currency translation on both revenues and earnings than we previously anticipated. On a constant currency basis, revenues would otherwise be up 5% to 6%.

The release touched on first half versus second half comparisons and pointed out that the investments that we have discussed with you in the past two calls are more heavily weighted toward the second half. Now, the investments made to date are already paying off, which you can clearly see in today's results. And we're highly confident that we're spending against the right initiatives to sustain growth through the balance of this year and into next year. Also bear in mind that our second half results will include a \$0.10 negative impact from foreign currency translation. So in a constant currency basis, we're now expecting revenue growth of 7% in the second half with earnings per share rising by approximately 5%, and that includes the higher brand spending.

You need to understand this spending is not just short term advertising, it's also, in longer term, brand and product development. For example, we continue to invest in new product innovation at The North Face where we're on a winning streak of product innovation awards. In the past year, The North Face has received more than 25 product awards. These include things like at the El Lobo pack, which was voted as the most stable pack by Backpacker magazine. And the Thunder jacket, an ultra lightweight

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high powered down jacket chosen as the editor's pick for 2010 by Trans World Snowboarding. And the Single Track lightweight training and racing shoe which was voted the Best Debut in 2010 by Runner's World. More recently, on July 15, North Face won three additional outdoor industry awards at the outdoor trade show in Friedrichshafen, Germany.

Now, I think it's important that I address a recurring question that is creating a lot of interest and concern across the industry. The credit relates to product cost inflation and potential impact on gross margins for both this year and next. Over the past couple months, we've been very consistent in our response to this question, so just want to reiterate that response here. Our product costs will be down in 2010 versus 2009. They were down in the first half of the year and they will be down in the second half of the year as well, but by a lesser amount. Gross margins are expected to reach a record high this year. Gross margins were substantially higher in the first half of 2010 compared with 2009, and we expect positive gross margin comparisons in the second half of the year as well. The gross margin increase will be less in the second half than what we experienced in the first half, which is consistent with the expectations we laid out at the very beginning of this year, so cost inflation is really more of a question for us in 2011. And we're not immune to the cost pressures that are occurring that stem primarily from the current imbalance between supply and demand. When demand dropped sharply beginning in late 2008, a lot of capacity, manufacturing capacity, capacity at the fabric mill, capacity in the shipping fleet and with containers, some of that was closed and some of it was just reduced.

But a pick up in demand began earlier this year and in fact, total apparel imports this June were 30% higher than last June and capacity has not yet caught up, which is driving increase costs across the board. Give you some examples. In terms of fabric, prices could be up a few percentage points next year with cotton the biggest driver for us, given our large jeanswear business. Cotton is trading near an all time high, and demand is currently running in excess of supply, however, the August and September cotton crop is expected to be strong, that could provide some relief next year. Relative to freight, the log jam and steam ships and containers are showing some signs in clearing as more capacity is being added. But current predictions are that freight will continue to run higher in 2011. Finally, labor. You're all aware of the labor increases occurring in China, but there are also labor shortages in other countries. All of these factors combined point to an increase in product cost of a few percentage points next year. At the same time, following a to pick up in spending earlier in the year, demand does appear to be softening some. That could increase some of these -- ease some of these cost pressures. It's just too early to know for sure. Now, it will not come as surprise to you that we are taking action to address these increases and sustain our strong gross margins, and we have several factors working in our favor..

For example, we have more than a century of manufacturing experience in our owned and operated plants. That provides us with deep expertise in product engineering and factory management, giving us the ability to improve efficiencies to address some of these cost pressures. Also, our large, efficient and diversified global supply chain helps us. Less than 25% of our source product comes from China where severe wage inflation is occurring. That's a lower percentage than much of the industry. And we still own and operate about a third of our manufacturing, and our own labor cost and own facilities are stable. Next, our changing business mix is another long term positive for gross and operating margin. We've stated our intention to continue to expand our international and direct to consumer businesses. Expansion in both should continue to fuel higher gross margins in the future.

Gross margins in our Lifestyle brands, particularly those in our fast growing outdoor and action sports businesses, are well above our corporate averages. And as these businesses comprise a growing portion of our portfolio, we expect to see a corresponding benefit to gross margins. Finally, a word on pricing. Clearly, price increases will be part of the formula for protecting our gross margins in 2011. So in summary, yes, like the rest of the apparel and footwear industry, we are seeing some cost pressures. But we believe we have an advantage business model and a brand portfolio that will enable us to address these pressures. No doubt we'll have much more to say on this subject next quarter as visibility in all of these areas becomes more clear.

Before I turn the call over to Bob, I'd like to close by reiterating our confidence in the strength of the VF business model which has proven to be very resilient during turbulent times and will continue to serve as the foundation for the long-term growth and success of our Company. Our diversify of brands and geographies and channels of distribution and in sourcing continues to provide us with a competitive advantage as clearly demonstrated in the results we're announcing today. We've enjoyed an



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excellent year to date, but in true VF fashion, we are never completely satisfied with our performance. In the second half, we'll continue to invest aggressively behind our brands to drive growth and share gains, and we're looking forward to seeing these investments translate into strong revenue growth, record gross margins and all time earnings per share this year and position us for success in 2011. Now let's hear from

**Bob Shearer** - VF Corporation - CFO

Thanks, Eric. I'll start at the top with revenue. We are obviously really pleased with the 7% increase achieved in the quarter and as Eric noted, every coalition reported higher revenues. Also of note is that the 7% growth was negatively impacted by currency translation by 1 percentage point. Now, as we saw in the first quarter, our gross margin performance continues to be exceptionally strong. Our gross margins top 47% in the quarter with a 320 basis point improvement over last year's second quarter. Now as noted in the release, the improvement was driven by three primary factors. First, lower product cost, second, the continued expansion and improved gross margins in our retail stores and third, very clean inventories across our businesses. We expect that gross margins this year could slightly exceed 46%. Significant increase over the 2009 level, which was our previous all-time high.

SG&A as a percent of revenue rose by 70 basis points and nearly all of the increase was due to the higher marketing investments that we discussed, both in February and also in April. Marketing spending rose 19% in the quarter as we continued to invest behind a targeted list of high growth, high profit initiatives. In addition, our SG&A continues to reflect the changing mix of our business. For the full year, we continue to expect that our ratio of SG&A to revenues will approximate 33.5% including, and of course impacted by the \$85 million of growth investments.

Operating margins rose in the quarter as well by 250 basis points to 10.6% from 8.1% in 2009. Terms of the bottom line, EPS rose by a very strong 47% in the quarter. And as we saw in the first quarter, lower pension expense helped earnings per share by \$0.05. Foreign currency translation wasn't really a factor in our results this year. So the point here is that the strength of our quarter was driven by the strong business performance across our brands. Regarding our expectations for foreign currency translation for the full year, you'll recall that our prior guidance was based on a euro rate of [\$1.33] for the remainder of the year. Our euro rate assumption for the last half of this year is now [\$1.23]. Accordingly, as compared to 2009 currency rates, the negative impact on revenues this year from currency translation is \$73 million, and the impact on earnings per share is a negative \$0.04

Now, it's important to note that the impact from our current euro assumption on the last half of 2010 is a negative \$0.10 per share. And the negative \$0.10 is primarily in the third quarter, which is a big quarter for international businesses. So the negative \$0.10 in the second half plus the positive \$0.06 in the first half, really, mostly the first quarter, gets us to the negative \$0.04 per share for the year. Now, a few points about our coalition results. Our outdoor and action sports business continued to power our top line with revenues up 12%. Revenues of The North Face and Vans were up 12% and 24% respectively, which is even stronger than the performance that we saw in the first quarter.

The North Face brand experienced strong growth domestically as well as in Europe and in Asia, and the brand's direct to consumer revenues rose by 13% in the quarter. So the growth is very well balanced across geographies and across the brand's wholesale and retail businesses. Vans' revenues was driven by 20% plus growth domestically and a near doubling of revenues in Asia. Clearly, the investments we've been making behind these brands are really paying off, and we expect that they'll continue to do so. Our outdoor and action sports businesses experienced another quarter of very strong profitability with operating margins expanding by more than two full percentage points to nearly 14% in the quarter.

We were very pleased to see return to revenue growth in our jeanswear business in the quarter, with healthy growth in each of our domestic businesses which includes mass market, Lee and western specialty. A 6% increase in our mass business was due to the strength in our core Wrangler and Riders brands. Previously, we indicated that first quarter comparisons were affected by programs that were discontinued in the second quarter of 2009. Now that impact is behind us and in fact, we're now looking

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forward to expanding space again in our Riders and Wrangler womens businesses as we benefit from a strong pipeline from innovative new products. These factors are expected to drive substantially stronger second half comparisons for our mass business in 2010. Our Lee brand in the US is also performing well. Revenue is up 2% in the quarter. Our successful Slender Secret stretch program has been expanded, we're looking forward to the launch both of Lee Premium Select products, both of which are expected to result in substantially stronger comparisons in this brand's performances in the second half.

Our sportswear business also returned -- resumed growth in the quarter with revenues up 5%. Nautica's wholesale business and our Kipling US business both achieved a double digit increase in the quarter. We continue to be pleased with the progress that we've made in improving the profitability of this business is reflected in the substantial increase in both operating margins and income in the quarter. Revenues of our contemporary brands coalition rose 18% with double digit growth across all brands, which was in line with what we indicated last quarter. We've seen some softening in the premium denim category in the last couple of months as overall consumer spending has weakened, so we are taking a conservative approach for this business for the balance of the year. Then wrapping up with image wear. A great story here with revenue and profit increases in both our image and license sports businesses during the quarter.

Now, we previously indicated that some strengthening in our revenues would result in a substantial improvement in our operating margins for this coalition, and you can see that in the quarter's results. Our competitive advantage from a quick response and replenishment capabilities is benefiting both businesses as demand improves. Well, that does it for coalition results. The release also touched on our international and direct to consumer results, so just a couple comments here. As expected, our international revenue performance strengthened in the second quarter with a 6% increase in constant dollars. Currency translation did hurt us by 3 percentage points, so the reported increase was 3%. Now as in prior quarters, our performance in Asia was a real stand out with revenue growth of 26% in the quarter with double digit growth in The North Face, Vans and 7 for All Mankind brands. We're on track with our retail store openings this year having opened 41 stores to date out of a total of 80 to 90 stores planned for the year. Our direct consumer revenues were up 7% in the quarter.

So let's move on to the balance sheet, which continues to be a real strength for VF. Cash and equivalents were \$540 million at the end of the quarter, and inventories were down 10% in prior year levels. By year end, considering the significant decline in inventories by the end of 2009, inventory levels should grow in line with sales. Our cash generation continues to be very strong, and we now expect that cash flow from operations will approximate \$850 million. We did put our cash to work during first half, repurchasing 4 million shares to \$318 million, and the total shares purchased were 1 million higher than what we discussed last quarter. We'll continue to evaluate the best uses for cash going forward. Acquisitions clearly remain our priority. Eric has pretty well covered outlook for the year, I'll just add a couple of other points. Our tax rate all-in should 25.5% for the full year. Our operating margins for the full year will reflect substantial improvement over 2009 to just below 13% despite the incremental growth investments, and capital spending for the year should remain pretty much on target at about \$110 million.

So in summary, we're really pleased with our results to date this year. Now to be sure, we do have some concerns about the overall environment for the rest of this year into next, but our results clearly indicate that strong, highly profitable brands with compelling products that speak to consumers' needs will continue to succeed, regardless of the external environment. Eric?

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**Eric Wiseman** - VF Corporation - Chairman, CEO

Thanks, Bob. Now let's wrap up with some comments with Carl Heinz Salzburger, Vice President of VF International. Carl Heinz?

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**Carl Heinz Salzburger** - VF Corporation - VP of CF International

Yes, thank you, Eric. Just to remind the group, my comments will cover our international businesses in Europe, the Middle East and Asia, the markets for which I have responsibility. On a constant dollar basis, total revenues in these markets were up nearly 4% in the second quarter. We enjoyed solid growth in our outdoor and action sports business, which is primarily The North Face and Vans. Our sportswear and contemporary brand business, which includes 7 For All Mankind, Napapijri and Kipling and



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in our Asia businesses. During the quarter, we also continued to improve profitability with operating margins of our international businesses rising more than 200 bases points.

Despite a lot of well publicized concerns regarding the market trends in Europe, our major brands continued to perform strongly. Year to date, The North Face stores have achieved double digit comp store growth, and fall bookings are up 25%. Vans stores have also achieved double digit comp store growth through the first half of the year, with fall and holiday bookings also up 25%. We have been steadily increasing our investments behind both brands to drive growth and market share gains in Europe and are very encouraged by the results we're seeing to date. Our 7 For All Mankind brand continues to expand in Europe with 24% revenue growth in the second quarter. Strong bookings and additional new stores should drive double digit growth in the second half of the year as well. New stores opened in the quarter included Milan, Berlin and (inaudible), and we're looking forward to opening our second store in Paris this quarter. We remain on plan to open a combined total of about 15 owned and partnership retail stores in key European cities this year. Napapijri brand also continues to perform very well with 7% revenue growth with constant dollars during the quarter, double digit comp store growth in the first half and fall bookings up 15%.

There were couple bright spots in our European jeanswear business in the quarter. Our Wrangler brand boasted moderate growth in constant dollar in the quarter. The brand's cutting edge marketing campaign continues to gain accolades, winning five awards at the prestigious Cannes International Advertising Festival. While the profitability of our jeans business continues to improve, overall, this business continues to be our most challenging.

The momentum continues in Asia with revenues up 26% in the quarter. We enjoyed exceptionally strong results in The North Face, Vans and Kipling business in China. While still relatively a relatively small market for us currently, we're also making very good progress in India, where revenues grew by more than 50% in constant dollars during the quarter. As you have heard us discuss in past calls, we have committed to a substantial increase in marketing in China this year. We are back to aggressively expand distribution in China, we have 40% targeted increase in door count by year end, 1,400 doors, which should help guide our goal of 25% revenue increase across Asia in 2010.

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**Eric Wiseman** - VF Corporation - Chairman, CEO

Thanks Carl Heinz. That concludes our comments. We'd love to hear your questions. And Stacy, could you open up the line for questions for us?

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## QUESTIONS AND ANSWERS

**Operator**

Of course, sir. (Operator Instructions) We'll take our first question from Kate McShane with Citi Investment Research.

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**Kate McShane** - Citi Investment Research. - Analyst

Thank you, good morning.

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**Eric Wiseman** - VF Corporation - Chairman, CEO

Hi, Kate.

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**Kate McShane** - *Citi Investment Research*. - Analyst

Eric, you commented that for cotton we may see a -- may possibly see an easing of prices in the cost of this commodity if the crop is strong in August and September. Will you still be negotiating prices at this point for spring of 2011 or will you be locked in by that time?

**Eric Wiseman** - *VF Corporation* - Chairman, CEO

We'll have some flexibility in later spring, kind of mid to late spring pricing. That depends on how good the crop is too, Kate. There's a couple pieces that move there that make your question a hard one to answer precisely. We will certainly have -- we have certainly established our pricing agreements through this fall. And depending on when it feels like the crop might be good, that will partially drive that, but it would be by mid spring at latest.

**Kate McShane** - *Citi Investment Research*. - Analyst

Okay. Great. Thank you. And just one more question on the cost front. I would expect that you would see more pricing in your jeanswear business just because of how much cotton composes of that category. Do you have any pricing power in your jeanswear business, that 30% of your total sales, or will we see more margin pressure in this category while you take price increases in other categories?

**Eric Wiseman** - *VF Corporation* - Chairman, CEO

We absolutely have some pricing options in our jeans business. One of the reasons we're so focused on a strategy of innovation is because we have learned over the past few years in particular when we create innovative products that consumers really want, they helped us sustain some revenue momentum during the recession, and we've charged a fair price for those things. In fact, our average unit price at Lee has gone up with the recession because we've been innovative. So the combination of innovation, the strength of our brand gives us some flexibility. But you're right, that is where we have our biggest pressure point. We have plenty of product categories that between the fabrics that go into the products and the locations that they're made aren't really experiencing inflationary pressures right now. So it's -- you know how diverse we are in our business mix, we're as diverse in the inflationary pressures.

**Kate McShane** - *Citi Investment Research*. - Analyst

Okay, great. Thank you. If I could squeeze one more in about SG&A and your spending in the back half of the year. I know you're not giving quarterly guidance, but can you give any kind of comments around how we should drive our model with SG&A spending Q3 and Q4, will we see more in Q3 going into holiday, or will we see more spending in Q4? Will it be evenly distributed?

**Eric Wiseman** - *VF Corporation* - Chairman, CEO

Kate, I can't answer that, but Bob would love to.

**Bob Shearer** - *VF Corporation* - CFO

Hi, Kate.





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**Kate McShane** - Citi Investment Research. - Analyst

Hi.

**Bob Shearer** - VF Corporation - CFO

For the second half of the year, the way to think about SG&A is that the ratio, the percent to revenues will be up just a little over 100 basis points, actually in each quarter. The marketing spent actually, when you do the math, in the \$65 million out of the \$85 million, and that's obviously a little abnormally second half weighted. It's more weighted to the second half than we'd normally expect to see. But the \$65 million actually would drive about 150 basis point of increase over that period of time, so there are some offsets, lower pension expense as an example, but we'll net down to just a little over 100 bases points per quarter.

**Kate McShane** - Citi Investment Research. - Analyst

Okay. Thank you.

**Bob Shearer** - VF Corporation - CFO

Alright.

**Operator**

Thank you. We'll take our next question from Jim Duffy with Stifel Nicolaus.

**Jim Duffy** - Stifel Nicolaus - Analyst

Thanks, good morning.

**Eric Wiseman** - VF Corporation - Chairman, CEO

Hi, Jim.

**Jim Duffy** - Stifel Nicolaus - Analyst

Couple of questions. Hey, Eric, so little bit of a history view here. If you look back historically, relationship between cost at the border, say and price at retail, has there been a linear relationship, or in times when you see cost go up, historically has it been difficult to pass that through at retail?

**Eric Wiseman** - VF Corporation - Chairman, CEO

Have to think about that a little bit. We have not had problems in, historically, in addressing substantially all of the pricing of the inflation we've seen coming at us, whether it was from labor or from other cost of goods. Over time, we have been able to address substantially all of it, and we expect that will be the case this year as well -- next year as well.

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**Jim Duffy** - *Stifel Nicolaus - Analyst*

Is that VF specific or based on your historical perspective, is that an overall industry dynamic?

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

No, I can only speak to VF specific. I know that we have such strong brands that are in great demand by consumers, that helps us address some of that. Our -- and how efficient we are, I mentioned in the call, a third of all production comes from factories that we own and operate, and we are not having labor inflation there, or we're able to offset it by efficiencies based on how well we run factory. So we're just not just not seeing it there. So I understand there's a really big question out there, but we're pretty confident that we have work to do and this story is not yet fully told, but I'm real confident in our team's ability to address substantially all of this.

**Jim Duffy** - *Stifel Nicolaus - Analyst*

Yes, given your sourcing base, it seems you're better insulated than many. You've begun the booking process with some of your brands for spring. Early days yet, but what are you hear from the mindset of retailers as you have those discussions?

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

There's caution back in people's voices right now in general about the market. They're -- the slowdown that we've all seen happen since, I guess second week in May, has had everybody ask, how confident should we be in placing spring orders. The good news for us, if you look at what happened during even the recession when there was more than just a little caution, there was widespread caution, we continued to get pretty good bookings from most of our business. You know that in 2008 we had a good revenue year.

Last year we are down 4% on the constant currency basis across our company. And we're pretty confident that we've got the right brands and right products within our brands to do better than most in that and in fact, as people are getting more selective about what they buy, they're looking to leading brands. And if you're looking to leading brands, you're looking to brands like Wrangler and you're looking at brands Vans and The North Face. So we're pretty confident about next year.

**Jim Duffy** - *Stifel Nicolaus - Analyst*

Great. And then final question for Carl Heinz, can you provide an update on your progress with Vans brand in China and some thoughts on the outlook on that business over the next couple of years?

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

Carl Heinz, you've got it?

**Carl Heinz Salzburger** - *VF Corporation - VP of CF International*

Yes, yes, I've got it, I've got it. Yes, thanks, Jim. You heard me saying that before we had a very, very strong quarter with Vans in China which nearly doubled the business. Vans, we see Vans as a big opportunity for us in China. We just started, basically, couple of seasons ago. We have very talented management on the spot, management that knows about footwear. And it's one of the brands which certainly will do better and become a big opportunity for us in China. We opening store, we have a -- stores are allowed. I can't quote what can happen longer term, but certainly, it's one of the top opportunities we have.

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**Jim Duffy** - *Stifel Nicolaus - Analyst*

Great. Thanks, and nice job.

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

Thanks, Jim.

**Carl Heinz Salzburger** - *VF Corporation - VP of CF International*

Thank you.

**Operator**

Thank you. We'll take our next question from Bob Drbul with Barclays Capital.

**Bob Drbul** - *Barclays Capital - Analyst*

Hi, good morning.

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

Hey, Bob.

**Bob Drbul** - *Barclays Capital - Analyst*

Eric, I just have some questions on the mass jeanswear business. There was a recently a change from the US business for one of your largest customers, and I was wondering if you saw any major strategic changes that might positively or negatively impact your business and some of the changes or the moves in your Rider and Wrangler business. Is that due to the change in strategy or anything we should think about?

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

Well, Bob talked about the acceleration of our progress and our mass jeans business during his comments and what's driving that. There are a couple of things. We have been talking for a while about programs that we lost with one of our large mass customers, and we are regaining some of those programs and permission, I think, to gain them all back. Some of them were in test, some of them are further than test in the full roll outs. So that's to our team's tenacity and not giving up on those programs because we believe they were the right things for that customer. And we're giving permission to, at minimum test them and at best case, roll them out.

You've heard comments about one of our customers talking about returning to basics and they specifically mentioned things like jeans and tees. Any time we have a large customer mentioning a focus on jeans when we're their largest provider of national branded jeans, that creates an opportunity for us, and we're working very closely with that customer to help them get back to the more basic apparel business. I think it's the right move for them, and they'll execute it really well. We're really confident they can execute that well, and we're happy to be a partner in that with them.

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**Bob Drbul** - Barclays Capital - Analyst

Great. And Bob, I have a question for you. On product cost, I think Eric said that you would have lower product cost for the remainder of the year. I think in previous calls you had mentioned that you thought you would have higher year-over-year cost beginning in the fourth quarter. What has changed from that perspective?

**Bob Shearer** - VF Corporation - CFO

Well, that comment, Eric's comment was for the second half, so the cost, as you might expect, Bob, increasing a little bit as each quarter goes on. So for the fourth quarter, what I've indicated in the past is that cost -- product cost, when you compare it year to year, fourth quarter to fourth quarter of last year, right, that the cost will be up just a little bit over where they were last year. In the third quarter they will still be below, and that nets to just being slightly below for the second half of the year. The reality is that costs year to year, when you look at the second half of 2010 versus the second half of 2009, again, down a little bit on net basis, but fairly neutral.

**Bob Drbul** - Barclays Capital - Analyst

Okay, and then just one final question for Carl Heinz. On the strong bookings that you talked about within the European business, do you think there's much risk to those bookings at this point in time?

**Eric Wiseman** - VF Corporation - Chairman, CEO

Carl Heinz?

**Carl Heinz Salzburger** - VF Corporation - VP of CF International

Yes Bob. Historically we have seen, especially on the brands I mentioned where we have that strong bookings, that the cancellation rate is pretty modest. Now we haven't seen in the first semester a change of that cancellation rate, so honestly, we don't expect major surprises on those strong bookings, even for the second semester.

**Bob Drbul** - Barclays Capital - Analyst

Great. Thank you very much.

**Eric Wiseman** - VF Corporation - Chairman, CEO

Thanks, Bob.

**Operator**

Thank you. We'll take our next question from Omar Saad with Credit Suisse.

**Omar Saad** - Credit Suisse - Analyst

Thank you. Great quarter guys.

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**Eric Wiseman** - VF Corporation - Chairman, CEO

Thanks, Omar.

**Omar Saad** - Credit Suisse - Analyst

Wanted to ask a question on priorities for cash flow. It looks like you're buying back stock more aggressive than you have in the past. What are the key decision factors there? How are you thinking about buying your own brands versus buying -- going out on the M&A market and picking up some brands? And I also have a question on the marketing and advertising spend. I thought you made an interesting comment that you're seeing a nice pick up in the areas where you're spending marketing -- spending on marketing and advertising dollars. Can you give some more color there and how that makes you feel about where the consumer is?

**Bob Shearer** - VF Corporation - CFO

Omar, I'll start on the first part of the question relative to priorities for cash. We did. We expected to buy back 3 million shares in the first half of the year, and that was our communication. And when the market fell off a little bit -- as the market fell off a little bit, we were seeing strengthening in our cash generation for the year and our cash position, the resulting cash position. So it felt like we could and should go out and buy an additional million shares. Having said that, our priority, as I said in my comments, our priority remains on the acquisition front. That is with we want to invest, and that's been pretty consistent over a period of years. So we saw the opportunity, we upped the buyback a little bit, even in the second half of the year. We could do a little more from that standpoint. But it's not a change in strategy or focus. Our focus remains on the acquisition front. Eric, do you want to take --

**Eric Wiseman** - VF Corporation - Chairman, CEO

Yes, Omar, I'll deal with the second part of your question which is about where we're seeing improving results from investments we've made in the business this year. I'll give you a couple of examples. One is the Nautica Father's Day TV campaign that we ran in partnership with Macy's. We did that in two markets as a test. We did that in New York and we did it in Florida. I won't give you specific numbers because I'd rather keep those -- that as internal information. But they were very encouraging, enough so that we're hoping to do more of that and increase that investment with Macy's later on this year. Another is Van's in Europe where we, in June I guess, ran an outdoor campaign in several cities. I think we were in six or seven cities, and Carl Heinz, correct me if I get this wrong, we did, in some cases, just a lot of outdoor billboards. And we took a few markets and did big splashes of Vans awareness, talking about the history of the brand and the products that we sell. And we saw an immediate lift in both our sell through at retail and in immediate bookings. One up -- Carl Heinz, do you have any color to add to that comment about Vans?

**Carl Heinz Salzburger** - VF Corporation - VP of CF International

No, you said it all, Eric.

**Eric Wiseman** - VF Corporation - Chairman, CEO

Okay, And the last example I'll give you, in the script, Omar, I talked about the product awards we're getting at The North Face. We are making substantial investments in both consumer insights to inform us about the products that we should be making, in our business model around the activity based model and in people to help to create really compelling product. And some



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of that shows up in awards. I also shows up in momentum with your brand. And for us to keep a brand that big going, we have to continue to create amazing products. So we're investing in that, and that's a long term investment. Is that enough examples?

**Omar Saad** - *Credit Suisse - Analyst*

No, that's great, thanks. Good job.

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

Thank you.

**Operator**

Thank you. We'll take our next question from Sean Naughton with Piper Jaffray.

**Sean Naughton** - *Piper Jaffray - Analyst*

Hi, guys. Vans, obviously a great quarter. Can you talk about the domestic growth? I think you said it was up 20%. Can you walk through the combination of that growth, whether it's through new doors or the introduction of new doors of the brand or comp store growth and how the comps were within your existing wholesale accounts for Vans domestically.

**Bob Shearer** - *VF Corporation - CFO*

Hey Sean, this is Bob. Most of the growth by far, about 75%, actually, of the growth came from or wholesale business. So the remainder was primarily from opening new stores. So again, just a great story abounds, just an incredible quarter and year so far. And especially in the fact that most of that growth has been driven by the wholesale side of things.

**Sean Naughton** - *Piper Jaffray - Analyst*

Yes, and then has there been any change in the penetration of apparel and footwear? Are you still tracking kind of in that 70, kind of 25 range?

**Bob Shearer** - *VF Corporation - CFO*

It's still tracking pretty close, pretty close to where it was on the wholesale side. A little bit more of that is on the -- is in the apparel side of the business. So it's getting a little bit of strength, it is gaining some strength. But still, overall for the brand, pretty close to where we've been.

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

And Sean, the thing I would add to that is, Carl Heinz just talked on answering another question about Vans' success in China, and I just mentioned our investment in Vans in Europe in select cities. The Vans brand, we are highly confident it can continue to grow and we are investing in it to deliver that growth. It's a very strong brand.

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**Sean Naughton** - Piper Jaffray - Analyst

Great. And then -- thanks for the detail on the sourcing front by the way, Eric, that's very useful. But can you discuss any, are there any delays or anything you're seeing within the supply chain right now where you guys are having trouble getting the goods that you've placed order for the fall are getting here domestically?

**Eric Wiseman** - VF Corporation - Chairman, CEO

Yes, the -- we're not -- so we don't have huge challenges there. There is a shortage of both ships and containers, but during non-peak times, just in normal kind of fall demand, we're pretty con -- we're having to scramble during really peak months where there's a lot of stuff coming at us. And that's true for back to school, so we're experiencing that now, and it will be true for holiday. What our experience has been for back to school is that we've been able to work around it, and we're having minor delays. A week delay getting stuff here, which does not affect our ability to get product to market. It's taking a whole lot more work from our supply chain team to get them here, but they are able to get them here reasonably on time.

**Sean Naughton** - Piper Jaffray - Analyst

Okay. Is it just a change in mix in terms of how you're importing in terms of air freight or anything like that? Are you having to increase that percentage of your -- of the goods that you're bringing in?

**Eric Wiseman** - VF Corporation - Chairman, CEO

Yes, a little bit more air freight for us this year. There's a surprising statistic, and I'm getting very granular here. But in a normal year, about 2 million new containers go into service. And some go out of service, right? They just -- they need to be removed from the chain. Last year, only 200,000 new containers went into service. So it was a 90% reduction in the supply -- introduction of new containers into the system, and that's what's creating a lot of this pressure right now. That industry is getting back and refilling that demand, but it's taking a while. As I said, we're able to work around it pretty well.

**Sean Naughton** - Piper Jaffray - Analyst

That's helpful, thanks. Great quarter, and best of luck in the second half for you guys.

**Bob Shearer** - VF Corporation - CFO

Thanks, Sean.

**Operator**

Thank you. We'll take our next question from Michael Binetti with UBS.

**Michael Binetti** - UBS - Analyst

Hey guys, good morning. Can you hear me okay?

**Eric Wiseman** - VF Corporation - Chairman, CEO

We can hear you great, Michael.

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**Michael Binetti** - UBS - Analyst

Congrats on a nice quarter there. So if I piece together a few of your comments from today, it sounds like you're fairly confident for some of the orders, at least in your key growth driver brands that you're seeing in early on discussions for 2010. And you think you have enough pricing power across the portfolio to help offset some cost inflation that everybody's starting to talk about. And you also pointed to the ongoing mix of the business. I know it's a little early to talk about 2011 at this point, but since you guys gave quite a bit of helpful detail looking at least into the early part of the year. Is there any reason at this point that we shouldn't expect gross margins for VF Corp to keep expanding in the first part of 2011 in our models?

**Eric Wiseman** - VF Corporation - Chairman, CEO

Yes, Michael. Well, as you said, we did provide a lot of details and a lot of color around the numbers. But it's still -- we just continue to believe it's just a little too early, right? It's just a little too early to comment on that. What we try to point out are all the pieces that we're looking at, all the areas of opportunities that we have, all the actions that we're taking to address that. But you will hear a lot more about 2011 in the very near future.

**Michael Binetti** - UBS - Analyst

Alright, then maybe I can just ask a question about North Face. I'm looking at the US business for North Face. Obviously, it's very back weighted for the profitability of that brand. Could you help us look at how the total -- how your order book looks for the US for North Face? And then maybe in particular how ASPs look on a year-over-year basis in the orders that you guys have on the books right now?

**Bob Shearer** - VF Corporation - CFO

Well, we talked -- the last time we got together actually, we talked about our order positions being, actually globally, up 20%. And that obviously is -- we haven't seen any fall off from that, so that business, as you said, continues to perform really well. And the order position that we're seeing for fall shipments remains quite strong.

**Michael Binetti** - UBS - Analyst

Any comment on ASPs?

**Eric Wiseman** - VF Corporation - Chairman, CEO

I don't -- we're not under any pressure. My guess is -- I don't know the answer to that. I won't guess that.

**Michael Binetti** - UBS - Analyst

Okay, thanks.

**Eric Wiseman** - VF Corporation - Chairman, CEO

Thanks, Michael.



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**Operator**

Thank you. We'll take our next question from Todd Slater with Lazard Capital.

**Todd Slater** - Lazard Capital Markets - Analyst

Thanks very much. Great quarter and report, guys.

**Eric Wiseman** - VF Corporation - Chairman, CEO

Thanks, Todd.

**Todd Slater** - Lazard Capital Markets - Analyst

Yes, I may have missed it, but can you tell us what the -- just how much Europe was up overall, maybe provide a little bit of color on some specific countries? And then just back to the ASP question, I'm just trying to get my arms around it. It sounds like you're planning to offset some, if not all of the sourcing and other cost increases with some pricing increases. And you talked about innovation and ways in you could achieve that. And I'm just wondering in the fourth quarter and maybe in 2011, should we expect your ASPs or unit prices to move up roughly in line with the sourcing inflation that exists, and if so, what would be good starting point? And then lastly you said that the retailers are getting a little more cautious, and just I'm wonder if you're seeing any of the -- if any of the big department stores have indicated that they might want to be a little more conservative on the back half deliveries?

**Bob Shearer** - VF Corporation - CFO

I'll start on a couple of those. We're both writing down as you're asking your questions, Todd. First of all, the international business I made a comment that our total international business on a constant dollar basis increased by 6% in the quarter. It was impacted by translation, so that pulled it down to about 3%. In terms of ASPs, yes, I think it is fair to assume that, as we've indicated, we clearly see pricing increase potential for our brands as we move into next year. So again, all things being equal, yes, we will see some price increases next year clearly across our businesses.

**Eric Wiseman** - VF Corporation - Chairman, CEO

On the question about are retailers getting cautious and how are we seeing that, we've had some very -- we've had very few instances of kind of cancellations and delays in terms of materiality to overall VF. So we have seen it's been very spotty, but it's not been a big issue or material issue in terms of a discussion we would have.

**Todd Slater** - Lazard Capital Markets - Analyst

Okay, and the international, I was curious about Europe specifically, if you could -- I got the overall international and I think you mentioned up Asia 26% and India up 50%. What was -- did you give us the European numbers and maybe talk a little bit about some of the specific countries and what you're seeing there.



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**Eric Wiseman** - VF Corporation - Chairman, CEO

I don't -- Bob and I are looking at each other, neither of us have specific numbers for Europe. Carl Heinz, do you want to talk about the PIGS countries and what's going on there and how much they are -- how important or unimportant they are to our overall mix?

**Carl Heinz Salzburger** - VF Corporation - VP of CF International

Yes, yes, yes. Clearly -- it's a lot, it's publicized a lot, the PIGS countries are not in the best shape, to come to the point. The good news is it's relatively modest business for us, so our exposure is relatively thin there. We haven't thought -- we haven't released a number for Europe, so what I can, we have three coalitions, three big businesses. One is outdoor and action sports, one is sportswear, the third one is jeans. And two are growing and one -- remember on jeans we closed the mass business last year. So we're showing negative growth, but it's not really comparable. But we did mention that Wrangler had good results in the quarter.

**Eric Wiseman** - VF Corporation - Chairman, CEO

Todd, does that help you?

**Bob Shearer** - VF Corporation - CFO

Todd, I can give you a little bit more on that. In constant dollars, our growth in outdoor and action sports was high single digit kind of growth. However, in our jeans business, that pulled that down. And so again, that business is still -- it's more stable than it was, but it's still declining a bit, even in constant dollars. So those are the two significant factors, but the point is our -- by far our largest business and fastest growing business there, which is our outdoor and action sports continues to grow at a nice pace.

**Todd Slater** - Lazard Capital Markets - Analyst

Great, that's very helpful. And just, are you going to -- when do we cycle that change in the mass piece? Can you just remind us when that is?

**Bob Shearer** - VF Corporation - CFO

Yes, that was a -- yes, it was about an \$8 million impact to the quarter, so not so big, not so big any more. And in the second half, just to carry through with that, in the second half just year, we had about \$20 million of revenues associated with that mass jeans business that we've now exited. So \$8 million in the second quarter and \$20 million for the last part of the year and then that will be done.

**Todd Slater** - Lazard Capital Markets - Analyst

Excellent, thanks that's very helpful.

**Bob Shearer** - VF Corporation - CFO

Thanks Todd.

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**Operator**

We'll take our next question with David Glick with Buckingham Research Group.

**David Glick** - *Buckingham Research - Analyst*

Good morning, and I want to add my congratulations on a great quarter. Just a follow up on Todd's question. Have you seen Carl Heinz, any change in trend over the last couple of months as given in all the headlines we've heard kind of mixed things about Europe. Just wondering if you've seen any deceleration in your European business. And secondly, just curious to what's driving the turn around in Nautica, which obviously showed some major improvement.

**Carl Heinz Salzburger** - *VF Corporation - VP of CF International*

Okay, the first question, David, we clearly stay very cautious, because a lot of rumors and a lot of facts are going around Europe, the economy, certain countries are not in the best shape, so we do remain cautious. Especially in our stronger brands, we have not seen negative signals. Our consolation rate has not changed, and I would say that the strong brands are doing well. While we stay cautious, we're pretty confident and don't expect negative effects happening the second semester.

**David Glick** - *Buckingham Research - Analyst*

Great, thanks.

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

And David, this is Eric. I'll deal with the Nautica turnaround. We're obviously thrilled that Nautica has had a really strong wholesale business in the first half. The team there has worked very hard over the last 18 months to get the right product assortment together, to get the right marketing communication methods together and to get the right -- to get that to come to life at retail with our retail partners in the right way. That's kind of firing in all cylinders right now. So they've had a really good first half and the business is turning more pure into their traditional wholesale department store channels, so that's all really, really good for us. The outlet stores there, I will tell you have not done as well, nor have they been our focus. Our priority was rebuild the platform for the wholesale business. Once done, leverage that into our outlet store model. So we're working on the second phase of that, and I would expect to see improvement in our outlet store business there

**David Glick** - *Buckingham Research - Analyst*

Are retailers now, given the turnaround this spring, starting to chase product for fall and increase their bookings on a relative basis for spring?

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

So I would say that our fall bookings, which are the ones that fall on holiday, which are the ones we have in hand, are significantly higher than the -- what we assumed they would be back in January and February before we began to get some momentum in the business. So our customers are increasing their support of the brand based on the performance this spring for fall and holiday. We don't have spring bookings yet, so I can't comment on that.

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**David Glick** - *Buckingham Research - Analyst*

Okay, great. Thanks a lot. Good luck.

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

Thank you.

**Operator**

Thank you. We'll take our next question from Robby Ohmes with Bank of America Merrill Lynch .

**Robby Ohmes** - *BofA Merrill Lynch - Analyst*

Oh, thanks. Just a quick question. I was wondering if you guys could give a little more detail on the growth driver outlook for North Face the way you did with Vans, meaning can you give us a little color on how wholesale versus retail looks for The North Face in apparel footwear versus accessories, sort of aligned by US versus Europe versus Asia, just to give us a flavor if anything is changing in terms of what the growth drivers look like for the overall brand. Thanks.

**Bob Shearer** - *VF Corporation - CFO*

Robby, I'll start on that. I gave some numbers for Vans relative to the breakout of retail versus wholesale, and it's very much a similar story for The North Face. As a matter of fact, even more so. Nearly all of the growth in The North Face that we've been seeing is due to the wholesale side of the business, not so much driven by new stores. And also from an international versus US standpoint, as we've been seeing and as we've been saying and as we look forward as well, the brand is strong. The brand is strong here in the US, it's strong in Europe and it's also strong in Asia as well. So we're seeing really equal strength, equal growth. We said previously that order positions for the fall business being up on the 20% area, again, that was -- we saw consistency across the globe relative to those positions. So that's, again, it's good news from all angles.

**Robby Ohmes** - *BofA Merrill Lynch - Analyst*

And any sort of category color, is footwear starting to really accelerate, or is it sort of apparel and footwear and accessories all moving together?

**Bob Shearer** - *VF Corporation - CFO*

I say mostly moving together. Our footwear business is still -- the resurgence, I guess I'd say, of our footwear business is still in some early stages as we've talked about in the past. But the areas that have shown strength and particularly on the apparel side continue to show strength. Not a big change there.

**Robby Ohmes** - *BofA Merrill Lynch - Analyst*

Got it. Hey, thanks very much.

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

Thanks Robby.

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**Operator**

We'll take our next question from Ken Stumphauzer with Sterne Agee.

**Ken Stumphauzer** - *Stern, Agee & Leach - Analyst*

Good morning everyone, thank you for taking my questions. Just briefly, on the direct to consumer segment there was a pretty noticeable deceleration on the year-over-year growth rate. What's causing that? Is it slower year-over-year increase in store?

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

The -- well, two things really. First is when we -- our store growth rate for the first quarter was 10% and when that happened, we said at the first quarter call, we did not expect to see that going forward. What we've learned in the second quarter was that it was slightly worse than we thought it was going to be. We knew it would slow down from that kind of rate. In fact, the second quarter, our comp store growth rate was about flat, it tailed off in the last six weeks of the quarter.

Our outlook for the year also came down by about 100 basis points in terms of our assumption about comp store growth, which we said would be mid single digits, and we're down about 100 basis points from what we thought sooner. We've been doing -- we've been opening new stores and closing stores, getting our mix to a position where we have a much more effective retail portfolio, and it's showing up in improved profitability in our stores. So while we have some comp store pressure from consumer spending, which I think we're not alone with, the profitability of our direct to consumer model continues to improve because we're getting the store mix right and exiting the under performing stores and investing in new stores and are still on track to open about 80 new stores this year.

**Ken Stumphauzer** - *Stern, Agee & Leach - Analyst*

Okay. Secondly, Bob, in the past you've disclosed kind of the order of magnitude of the different gross profit margin puts and takes. Can you do that again? What comprised that 370 basis point expansion?

**Bob Shearer** - *VF Corporation - CFO*

Yes, yes. In the second quarter, and as we've been talking about here, a different story than what we expect to see for the rest of the year because of the comparisons of the second half of the year against the second half of last year. So product cost, the reduction in product cost added about 200 basis points of the 320. Eric just talked about, and this is on gross margins, Eric just talked about our retail performance, and that has improved, and that contributed about 70 basis points. And just operating the business really cleanly and other mix factors and all those other kind of things made up the difference.

**Ken Stumphauzer** - *Stern, Agee & Leach - Analyst*

Okay.

**Bob Shearer** - *VF Corporation - CFO*

Go ahead.



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**Ken Stumphauzer** - *Stern, Agee & Leach - Analyst*

Actually, just moving on to the next question. You guys -- I know you can't talk in specifics, but as far as the M&A environment goes, we've obviously see a lot of volatility in the equity markets and perhaps some concerns in the credit markets. I'm just wondering if you're seeing perhaps valuations come down to more reasonable levels yet.

**Eric Wiseman** - *VF Corporation - Chairman, CEO*

I wish I could say that was the case. I think that has not been -- we have not gotten an acquisition done this year, so that's blinding flash of the obvious. Having said that, one of the reasons has been price. We have not been able to come to terms with the price that the sellers expect, and we don't have anything that I have as a reference point, but clearly the markets have come down, and that might suggest a different kind of valuation. We remain focused, as we have been, on the outdoor and action sports sectors as our primary focus for acquisitions, and we're still very active.

**Operator**

Thank you. We'll take our next question from Mitch Kumentz with Robert W. Baird

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

Thank you. A few questions, first on the gross margins. When you look at your outlook for the back half of the year, you guys are saying gross margins are up and product cost down, but Bob, you made the comment that you should actually see some product cost increases in the fourth quarter. So do you expect gross margins to be up in the fourth quarter, or is it more just so just the third quarter, or how are we be thinking about that between the two quarters?

**Bob Shearer** - *VF Corporation - CFO*

Yes, it's a little bit more improvement, just as you expect Mitch, with costs, what's happening with costs. And again, it's not a huge impact here, but yes, we expect to see the comparison a little stronger in the third quarter than the fourth quarter -- versus the fourth quarter last year that was really extraordinary quarter for us. So yes, clearly a little more improvement, yes, in the third than the fourth.

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

But you still think gross margin could be up in the fourth quarter even with --

**Bob Shearer** - *VF Corporation - CFO*

There will be -- possibly, yes, slightly, but flat to up very slightly.

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

Okay, thanks. Then on the SG&A, Bob, you mentioned that if you strip out your higher investments in the back half you actually expect leverage on that line item which is pretty impressive, I think, given that -- what's happening with mix, particularly as you build out your retail business. So I guess the question is on a longer term basis, how should we be thinking about that SG&A line&gt; Is that something where you can get leverage over the next few years? Is that how you're thinking about the business on a go forward basis?



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**Bob Shearer** - VF Corporation - CFO

I'd say relatively to SG&A, Mitch, that a lot does depend on our spending on the marketing spend. And you're right, what we're seeing this year is that the big factor is in fact the higher in the incremental marketing spent. Now to be fair, one of the points of leverage you could say, but our lower pension expense is helping us there, so that accounts for some of the difference. But still, otherwise, relatively flat. So I think a lot of that is going to have -- will depend on the marketing spend, and that's yet to be seen. If our marketing continues to -- the higher spend continues to produce the results that we're seeing, we may continue to accelerate the spend. So --

**Operator**

Thank you. We'll take our next question from Chris Svezia with Susquehanna Financial Group.

**Chris Svezia** - Susquehanna Financial Group - Analyst

Good morning everyone, and congratulations as well. I guess one of my questions is just on, if we can talk about 7 for a moment and just, Eric, your comment about what you're seeing in that business. Maybe talk about retail and the wholesale pieces in terms of what you're seeing there in terms of the business.

**Eric Wiseman** - VF Corporation - Chairman, CEO

Sure, that one shifted on us a little bit here in the second quarter. We had a really strong first quarter with them, we had a strong second quarter with 7 as well. We have seen a slow down in the premium denim space in the last few weeks -- last few weeks, in the last eight weeks really, since May. That segment in particular has been a soft spot, so our stores are still working for us and we're continuing to invest in our stores, but there clearly has been a sort of how long that lasts, I wish I knew the answer to that.

The answer for us is to make sure we create compelling product, which obviously we're working on that, and we're increasing our investment in brand. In fact we're just about doubling our marketing spend behind 7 For All Mankind right now because we think it's a great brand. And even though it's under pressure right now, we're going to spend on it to make sure that we connect with consumers in the right way. We underspent on it a bit in the last few years, so we're going to reinvest in it and hope we have the right products at the time and that the fall gets better than the last eight weeks have been.

**Operator**

Thank you. We'll take our next question from Dana Telsey with Telsey Advisory Group.

**Dana Telsey** - Telsey Advisory Group - Analyst

Hi, good morning everyone. As you think about the compet-- the contemporary business, even beyond 7, what are you seeing in terms of price points, department store contribution for in store shops? How is that moving along in their ordering trends? And just lastly, not just to the beat the dead horse in terms of product cost, as you think about 2011, do you see price points to consumers changing? Thank you.



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**Bob Shearer** - VF Corporation - CFO

Sure. In the contemporary space in terms of price points, there was a significant reduction in price points during the course of the recession over a two year period. The average price point for a pair of premium jeans, regardless of brand, came down. It didn't mean we didn't still offer the high end of the range, but the consumers bought more at the lower end of the range. So we saw a reduction in AURs. That stabilized in the first four months of this year, and I think it's under question right now Dana, because there's been a change that really has just happened. And as you know, we're also at a period of year, it's been a very warm June and July across the United States, and I'm not sure if people are waking up thinking I'm going to go buy a pair of long bottom jeans right now because that's what I want to wear today. In fact, I'm pretty sure they aren't.

The question will be during back at school, does that come back and what does that mean to the average unit retails? Your question about 2011, I wrote 2011 on my pad, I can't remember your question. Was it about -- oh, it was about pricing? Pricing. I think we're going to see some modest increase in price points across many apparel brands, including ours, to offset some of the inflation we're seeing in the -- inflation is real. The labor rate and cotton inflation, that's real, and I think we're going to see every apparel company try to figure out how to deal with that, including reflecting some of that in their pricing to consumers.

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**Operator**

Thank you. And we'll take our next -- our last question today from Kevin Boler with Morgan Stanley.

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**Kevin Boler** - Morgan Stanley - Analyst

Hey, thanks for taking my question. Hey, Bob, you've taken a couple of questions today on M&A and I think in particular, you're saying that some of the targets are maybe asking too much here. But I think in March you mentioned that you'd be willing to make \$1 billion plus acquisition if you could find the right target. I'm curious if you are still thinking that \$1 billion plus is a good number and just what your constraints are. How do you think about your capital structure? Is there -- with leverage now close to one turn, is it -- is three or four turns too much leverage for the right acquisition, for a \$2 billion or \$3 billion or \$4 billion acquisition? I'm just curious, what are the constraints to how you think about a capital structure how low do you want to keep leverage, and how do you think about the big picture Cap structure questions as you think about M&A.

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**Bob Shearer** - VF Corporation - CFO

Yes, Kevin, we do talk about a \$1 billion deal because we could clearly afford to do that, and that's really where the comments are coming from. So we often get the question, would you could you do \$1 billion deal? And we say, well, we certainly could, and we would for the right brand. All the risk factors would have to be appropriate to do the \$1 billion deal, but we would do \$1 billion deal.

So our debt -- when you look at our debt ratios right now and our cash position as well, it obviously gives us a lot of flexibility. We talked a little bit earlier, don't know if you heard it, there was a question relative to the buyback program. We upped the buy back a bit here in the quarter over what was expected. We bought back 4 million shares versus the 3 expected, said we could increase that a bit as our cash continues to strengthen. So I think the bottom line, Kevin, is we just have a lot of flexibility in our balance sheet right now from a cash, from a debt standpoint and the priority remains on acquisition. We could do a larger acquisition. If you looked at our history it would say that that's not as likely as one that's below that \$1 billion mark.

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**Operator**

And that was our last question. I'd like to turn the conference back over to Eric Wiseman for any additional or closing remarks.



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**Eric Wiseman** - VF Corporation - Chairman, CEO

Yes, thanks everyone for joining us. We're obviously pleased with the second quarter. That is history now. More importantly, we're confident we can navigate the challenges ahead of us, and we look forward to keeping you updated as we do just that. Thanks so much. Bye-bye.

**Operator**

Thank you. Ladies and gentlemen, this does conclude our presentation. We appreciate your participation. You may now disconnect.

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