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Caleres, Inc. (CAL)

Q2 2017 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon. My name is Ian, and I'll be your conference operator today. At this time, I'd like to welcome everyone to the Second Quarter 2017 Caleres Earnings Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions] Thank you.

I'd now like to turn the call over to Ms. Peggy Reilly Tharp. Ma'am, you may begin your conference.

Peggy Reilly Tharp
Vice President, Investor Relations, Caleres, Inc.

Thank you, Ian. Good afternoon. I'm Peggy Reilly Tharp, Vice President of Investor Relations for Caleres, and I'd like to thank you for joining our second quarter 2017 earnings call and webcast. A press release with detailed financial tables and slides are both available at caleres.com.

Please be aware today's discussion contains forward-looking statements, which are subject to a number of risks and uncertainties. Actual results may differ materially due to various risk factors including, but not limited to, the factors disclosed in the company's Form 10-K and other filings with the U.S. Securities and Exchange Commission. Please refer to today's press release and our SEC filings for more information on risk factors and other factors which could impact forward-looking statements. Copies of these reports are available online. The company undertakes no obligation to update any information discussed in this call at any time.

Joining the call today are Diane Sullivan, CEO, President and Chairman; Ken Hannah, Chief Financial Officer; and Rick Ausick, President, Famous Footwear. And I would now like to turn the call over to Diane Sullivan. Ma'am?

Diane M. Sullivan

Chairman, President & Chief Executive Officer, Caleres, Inc.

Thanks, Peggy. I'd like to begin by saying a good start to the year continued into the second quarter as we reported adjusted earnings per share of $0.48, up 4.3% year-over-year. Consolidated sales were up 8.7%, including Allen Edmonds, and up 2% on an organic basis.

At Famous Footwear, comp sales were up 2.8% in the second quarter and were positive for each month of the quarter. In total, we saw improvement in sales across all genders, all climate zones and all consumer channels. We also saw an improvement in traffic, which was up 3.5%. And both comp sales and traffic are benefiting from our consumer-targeting efforts which I'll talk more about in a few moments.

In terms of product trends at Famous, we saw continued growth in overall athletic sales with men's and women's up mid-single digits, while kid's athletic sales were up high single digits. Lifestyle athletics also continued to trend higher and delivered sales improvement of 20%. For seasonal products, women's foodbed and sport sandal styles performed especially well in the second quarter.

In total, women's sandal sales were up low single digits and delivered significant margin improvement. For our Brand Portfolio, total sales were up 16.8%. It will come as no surprise that Sam Edelman and Vince, both women's and men's, had outstanding quarters, and we're seeing a growing level of enthusiasm for both of these brands.

We're also seeing progress at Naturalizer with North American sales up year-over-year. This brand continues to improve its overall performance as the work we've been doing is showing progress and promise. While we had planned for organic Brand Portfolio sales to be up low single digits in the first half, excluding Allen Edmonds, results came in flat as we continued to diversify our sales to shift away from lower margin channels.

At the same time, our focus on growing our e-commerce-related sales is delivering results. And these sales now represent nearly a quarter of our Brand Portfolio. So, solid results all around for both sides of our business.

But before I turn things over to Ken, I'd like to provide an update for a few key strategic areas that I've discussed with you before. First, our Allen Edmonds integration remains on track. For the quarter, the brand contributed to both our sales and gross margin improvement. In addition, we brought our new talent to lead Men's, including Allen Edmonds and International. We believe both of these areas represent untapped potential as we continue to diversify our portfolio.

Joining our company is Malcolm Robinson, who brings deep experience in Men's and in managing global brands to Caleres. He will oversee the strategic growth initiatives primarily for Allen Edmonds and the expansion of our International footprint.

Also new to Caleres is Akram Eldemachki who joins Malcolm and will lead the International team on a day-to-day basis. Akram will be supporting and building the international presence for all brands across our portfolio, but with a specific focus on Naturalizer, Allen Edmonds and Sam Edelman.

Our speed-to-market initiative also remains on track. The program has already helped us to improve our Brand Portfolio profitability and our ability to respond to consumer demand. It has also begun to drive improved retail sell-through and has enabled us to get early reads on our best-selling items. We believe this ongoing initiative will drive continuous learning and improvement for all of our brands.

Next, turning to Famous Footwear where we are seeing results from our strategic initiative to focus on acquiring, retaining and growing our share of wallet with targeted high-value customers. This work has provided significant consumer insights and, as a result, we have seen our best start to back-to-school since 2013. Season-to-date comp sales are similar to our second quarter as we've benefited from several key efforts related to these consumer insights.

For example, to drive consumer interest earlier in the season, we introduced trend stories in advance of the peak selling weeks and highlighted color trends, specifically gold, flesh and burgundy. We also rolled out new digital brand landing pages for our key athletic brands that we carry.

We also targeted media and marketing spend, which helped us to become more efficient and enabled us to react more rapidly. For example, this May, we completed a media test targeting prospective consumers. And based on the program's success, we decided to expand this outreach across the country for back-to-school.

As a result of these efforts, we're building relationships and engaging with new consumers by speaking directly to them, and these purposeful efforts are paying off and driving new visitors and shoppers to Famous Footwear. While it's still very early, we are working hard to own that relationship with our consumer. And we're seeing initial results and improved sales and traffic trends and increased rewards member signups in addition to a number of other areas.

While that covers some of the strategic work we're doing at our two business segments, I'd like to provide a quick look at our strategy from a corporate perspective. As in the past, we remain as efficient as possible and maintaining our financial flexibility is just one of those efforts. Our financial flexibility allowed us to complete the Allen Edmonds acquisition and further diversify our business and become a more balanced portfolio company.

I'm pleased with the progress we've made in continuing to grow our portfolio and in delivering a more balanced division of earnings, too. Both of the businesses in our portfolio have done just a great job of day-to-day execution in the short term, while maintaining focus on our long-term strategies and investments.

We remain confident in our ability to drive results and believe we have the right strategy, plan and people in place to consistently deliver as we have in the past. However, as we are still in the midst of our biggest quarter of the year, we are maintaining our fiscal earnings per share guidance at this time.

Now, before I turn the call over to Ken. I want to send our thoughts out to the more than 200 associates working and living in the Greater Houston area. This is a major market for us with employees from our Famous Footwear, Naturalizer, Allen Edmonds and Sam Edelman stores all being affected. We're monitoring the situation closely and hoping for the best for all of the people impacted by this very tough situation.

And with that, I'll turn things over to Ken.

Kenneth H. Hannah

Chief Financial Officer & Senior Vice President, Caleres, Inc.

Thank you, Diane, and good afternoon, everyone. I'm pleased to report that for the second quarter, we delivered adjusted earnings per share of $0.48 excluding $0.07 per share related to the acquisition, integration and reorganization of our men's brands. For the second quarter of 2016, net earnings were $0.46 per share. Our consolidated net sales for the second quarter of this year were $677 million, up 8.7% over last year. Our e-commerce-related sales, we saw double-digit sales growth on a year-over-year basis.

For our Brand Portfolio, second quarter sales of $272 million were up 16.8% versus the prior year and includes $41.8 million of sales from Allen Edmonds. Year-to-date, Brand Portfolio sales were flat versus 2016 excluding Allen Edmonds. At Famous Footwear, second quarter sales of $404.9 million were up 3.8% over 2016 as we operated 11 more stores year-over-year. Our comp store sales were up 2.8% for the quarter.

Now, turning to consolidated gross profit, which came in at $287.5 million for the quarter, gross margin of 42.7% improved 108 basis points, excluding $1.9 million of acquisition-related Allen Edmonds inventory adjustment amortization cost. Year-to-date, our adjusted gross margin of 43.1% was up 104 basis points, consistent with the second quarter.

Year-to-date Brand Portfolio continued to drive strong contributions to our consolidated gross margin, delivering 394 basis points of improvement, excluding our Allen Edmonds inventory adjustment and amortization cost. Organic gross margin was up more than 200 basis points versus the first half of 2016 with contributions from both our Healthy Living and Contemporary Fashion businesses.

For Famous Footwear, second quarter gross margin of 45.3% was down 21 basis points for the quarter, reflecting, in part, a year-over-year shift in back-to-school promotional efforts at our outlets. However, as you may recall from our first quarter call, we began offering buy-online, pick-up-in store in mid-May. By mid-June, we had rolled out to all doors and begun to see a favorable impact on our e-commerce gross margins.

Our total SG&A in the second quarter was 37.5% of sales or $253.5 million, including nearly $20 million of expense from Allen Edmonds. Excluding Allen Edmonds, our Brand Portfolio SG&A expense was up 6.5% year-over-year, primarily reflecting increased investments at Sam Edelman.

For Famous Footwear, we were able to leverage SG&A expense by [ph] 52 basis points (12:08) as the team delivered great top line for the quarter, ahead of expectations, and as we operate 11 more doors year-over-year. We anticipate further expense leverage in the back half of the year as we will close approximately 50 doors following the back-to-school season. Consolidated operating earnings of $35.9 million were up 11.2%, excluding $4.8 million of expense related to the acquisition, integration and reorganization of our men's brands.

Adjusted operating margin of 5.3% was up 12 basis points year-over-year. Famous Footwear delivered operating margin of 6.2%, up 41 basis points year-over-year. Our depreciation and amortization was $16.4 million in the second quarter, up 22.2%. This increase includes, among other items, the addition of Allen Edmonds and its retail doors; the Lebanon distribution center modernization and expansion; and the operation of 11 more doors of Famous Footwear on a year-over-year basis.

Net interest expense for the second quarter was $4.4 million, up nearly 40% year-over-year, reflecting borrowings against our revolving credit facility to finance the acquisition of Allen Edmonds in December of 2016. Our consolidated corporate tax rate was 33.9% in the second quarter and 31.7% year-to-date versus 32.3% and 31% in the same periods a year ago. Capital expenditures were $15 million for the second quarter. For the first half, capital expenditures of $27.4 million were down $3.8 million year-over-year.

Now, turning to our balance sheet highlights, we ended the quarter with cash and equivalents of $52.9 million. Outstanding revolver borrowings at the end of the second quarter were $35 million, down 68% from $110 million at the end of last year as we continue to pay down our revolving credit facility with strong cash flow from operations following the acquisition of Allen Edmonds.

In total, we delivered a 5.3% increase in cash from operations on a year-to-date basis. And by the end of the second quarter, we had paid down $220 million of the $255 million related to the acquisition of Allen Edmonds. In total, we repatriated $120 million and also used $100 million of the operating cash flow we've generated since the acquisition. While we still have approximately $35 million related to the Allen Edmonds acquisition remaining on our revolver, we expect to completely pay off this amount by the end of the year.

Our consolidated inventory position at quarter-end was $722 million, up 11.3% year-over-year, including Allen Edmonds. At Famous Footwear, we ended the quarter with inventory down 1.4% per store on a dollar basis and down 1.3% per store on a pair basis.

For our Brand Portfolio, inventory was up 39.6% including Allen Edmonds. Excluding Allen Edmonds, inventory was up 11.9% with the increase reflecting investments in key brands and styles at our growing drop-ship business.

I'm very pleased with our performance in the second quarter. We grew our top line 8.7% and saw improvements year-over-year in both adjusted gross and operating margins. We continue to maintain our financial flexibility, paying down the revolver borrowings related to our acquisition and we were upgraded by Moody's in the quarter to a Ba3 level.

Before we begin our Q&A, I'd like to reiterate our fiscal 2017 guidance which has not changed since we first issued it back in mid-March. Our consolidated net sales of $2.7 billion to $2.8 billion, comp sales of Famous Footwear, up low single digits. Net sales for the Brand Portfolio segment up in the high teens including Allen Edmonds. Gross margin up 45 basis points to 55 basis points. SG&A expense as a percent of sales up 30 basis points to 40 basis points, an effective tax rate of between 31% and 33%, an adjusted earnings per diluted share between $2.10 and $2.20, excluding approximately $0.13 of acquisition, integration and reorganization costs in the first half of the year related to the Allen Edmonds acquisition.

This guidance includes the closing of 70 Famous Footwear stores and the opening of approximately 40 new doors as part of our normal lease renewal process. The closing of approximately 11 Naturalizer stores and the opening of four new locations, the opening of 10 new stores for Allen Edmonds and one for Sam Edelman, depreciation and amortization of approximately $60 million, capital expenditures of approximately $55 million and an additional $12 million of operating expense related to the 53rd week in 2017.

As a reminder, due to the Allen Edmonds acquisition, we expect earnings per share to be more heavily weighted to the fourth quarter versus prior years. Additionally, we expect third quarter earnings per share to grow at a rate consistent with what we experienced in the second quarter of this year.

And with that, I'd like to turn the call back over to the operator for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question is from the line of Jay Sole. Jay, your line is open.

Jay Sole
Analyst, Morgan Stanley & Co. LLC

Q

Great. Thanks so much. Just want to start on Famous Footwear a little bit. With comp up 2.8%, can you just talk about maybe what new brands contributed to that comp and how much of a factor that was in the quarter?

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.

A

Yes, Jay. It's Rick. Obviously, the biggest new brand we had was Under Armour. And basically, when we looked at that business going into the purchase and to the back half of the year, we assumed that half of it would be incremental and half of it would be – come from other parts of our business. All I'll say is, without giving some more specifics, it's about, it's not any worse than that. That's about what it is. Might be a little less incremental than that, but we'll have to wait till we get to the end. It was semi-significant, less than 1%.

Jay Sole
Analyst, Morgan Stanley & Co. LLC

Q

Okay. And, Rick, can you maybe just talk about by month and what you saw at Famous Footwear and what your early read on back-to-school is having seen most of August at this point?

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.

A

So, we had a slight increase in May, low single digits in June, and a mid-single digits in July. That's how the flow went for the three months. And right now, we're kind of in that low to bottom end of mid-single-digit number for back-to-school.

Jay Sole
Analyst, Morgan Stanley & Co. LLC

Q

Okay. And then maybe can you just talk about what impact the hurricane might have on your business? Obviously, Diane expressed a lot of concern for all the people in that area. How do you think it's going to affect the business, if you could maybe give us anything about that?

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.

A

Yeah, it's hard to tell. I mean, part of it is about how long it takes and how before they can start getting back to somewhat normal. We have – Famous, we have 28 stores. I think, totally, we have something in the neighborhood of 38 or 39 stores.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

38, 39, right.

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.
A

And...

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.
A

It's about 2% of our total business.

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.
A

Yeah. So, it ends up to be a question of how do we – when could we get them back in order. We already know that there's some damage in a handful of them, but we don't know to what extent. Obviously, the problem right now is people still can't get around the city and the last thing we want them to do is worry about our stores when they're trying to take care of their families and things like that, Jay. So, I think it's a little early to – it's a top 10 market for us. So it could be reasonably significant. But we'll have to wait and see.

Jay Sole
Analyst, Morgan Stanley & Co. LLC
Q

Okay. And then maybe just one more for me. Just big picture perspective. Comps across retail have been still volatile and your delivery [ph] to the comp (20:38) is probably going to be better when all earnings season has done better than most. [indiscernible] (20:41) a better handle on why comps are moving so much and that's giving you a little bit better visibility into the business?

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.
A

Well, I can't speak for everybody else, but just about us. I think we've been on this path for a while. If you remember, couple of years ago, at an Investor Day, we talked to you about this high-value customer that we thought had – we had an opportunity to be better positioned against and we thought we were building some insights to. And we wanted to make them a bigger part of our business.

So, what we've – we have not varied from that. Our work – we've continued to work on all aspects of that over the last two years. So how we train our associates to approach customers in store, how we craft and word the messages we send out to our customers, what brand intensifications and product categories we impact in our stores. That's been the work we've continued to do and among other things.

The most recent thing that we did was find a test method – we tested some ideas on how to deliver the message directly to the consumer in a different way. That's what we were – that's where we have seen some return on that activity. The good news was we were able to take what we learned between May and early July and impact that into our back-to-school marketing plan starting the middle of July through August and into early September.

And as we look at it, those are the things that I believe are driving our results to be better than other people, and I think that's kind of the thing we're going to focus on. We believe there's still – we're in the very first early phase of this. But we think there's something to it. We thought that for a while.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.
A

Yeah, Jay, it's Diane. I'd just add a couple things to what Rick said. All of that is totally true and we've had to really stay the course on this because we did believe that, at the end of the day, it was always going to be about our ability to engage, retain and grow our customer base. That was the way that we were going to grow the business over the longer term. I think the other thing about this is – and I think we're just being a little modest on this, that the great execution and really picking the right categories to invest in have also made a difference in our business this year.

I think our footprint of being on average 6,500 square feet forces you to really think about what do you want to stand for and how are you going to make sure that you are – got the right assortment in that store with the right kind of depth that's going to be able to drive this kind of performance. So, I think it is that combination of this consumer engagement work we've been doing, how we stuck with it to try to get to the other side of it, and then it's just good old fashion, great execution by, I think, the Famous team in making sure that they had the right shoes in the right place at the right time, which still matters a whole lot.

Jay Sole
Analyst, Morgan Stanley & Co. LLC
Q

It sounds great. Thanks so much. Thanks, Diane. Thanks, Rick.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.
A

Yes.

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.
A

Yes.

Operator: And our next question is from the line of Jeff Stein. Jeff, your line is open.

Jeffrey Stein
Analyst, Northcoast Research Partners LLC
Q

Okay. A couple of questions. Nice job, everyone. It was a great quarter. So, traffic, you mentioned traffic for Famous Footwear was up 3.5%, and I'm wondering is that bricks-and-mortar only or are you including online? And if you are including online, can you kind of parse it out in terms of what the bricks-and-mortar traffic situation was?

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.
A

That was including all channels, brick-and-mortar as well as online. And you got it there? Okay. So, traffic was up, all-in, 3.5%, down 1% in brick and mortar and up 9%, a little over 9% at famous.com.

Jeffrey Stein
Analyst, Northcoast Research Partners LLC
Q

Wow!

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.
A

The [indiscernible] (24:35) is one of the best quarterly trends we've had in about five years.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

Yes...

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.

A

Basically, in mid-single digits. So, that was a relatively large move.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

Yes.

Jeffrey Stein
Analyst, Northcoast Research Partners LLC

Q

Excellent. Now, that's really good. Diane, maybe you could talk a little bit about how exactly you're engaging this high-value customer? Is it more through social media? When you say – digital encompasses a lot of different things, so maybe you could...

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

It sure does.

Jeffrey Stein
Analyst, Northcoast Research Partners LLC

Q

...give specifics in terms of what exactly you kind of landed on here in your test, your media test?

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

Right. I would say there is a couple of things, Jeff, and it hasn't – the communication piece of it and the marketing was the sort of last piece we put in place. It's been really understanding and identifying who these people are, understanding how we wanted to craft and create assortments of brands and products that they really like, so there was a lot of consumer insight that informed us about that.

It informed us a lot about our real estate and the location of where these high-value customers were around our stores which was a big piece of it. So, we can really see what the penetration of these customers are by market and by store, so we did a lot of that work. And then this last test was really a combination of a lot of different things and this is the interesting part about it, Jeff. We didn't really change the message or how we delivered it, it was the same kind of digital work whether it was e-com, email blast that we sent out, whether it was rewards messages that we sent out, it didn't really matter, it was the same vehicles, the same messages, but just to a much more targeted customer that fit into this profile of the high-value consumer.

So that was sort of this first step, and now we're going to get smarter and smarter and smarter about how we can actually specific and tailor different messages for each one of these different segments of our population.

Jeffrey Stein
Analyst, Northcoast Research Partners LLC
Q

Do you have any data on the average spend for a high-value customer on an annual basis relative to kind of the rest of the customer base?

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.
A

Yeah, we do...

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.
A

It's much bigger.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.
A

It's a lot bigger, yes. Let's see, I'm looking at this right now here. It's at least one – it's about our gold members, on average about 1.5 times what most will do. And our high-value customer is very close to what our gold member would normally deliver as well.

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.
A

[indiscernible] (27:22) highest level, yeah.

Jeffrey Stein
Analyst, Northcoast Research Partners LLC
Q

Do you have a number? How many high-value customers do you currently have?

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.
A

In our current database, we have a little under a million customers in our database right now. And that's – but that's been growing – I don't have the current numbers as we acquire new ones every day. So that'll be something we'll be able to keep track of, but we started with the – we've been harvesting somewhere in the neighborhood of a million customers. But now...

Jeffrey Stein
Analyst, Northcoast Research Partners LLC
Q

Growing, okay.

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.
A

...that number is growing obviously.

Jeffrey Stein
Analyst, Northcoast Research Partners LLC
Q

Great. And then a couple of additional questions real quick. First of all, the benefit of buy-online-pickup-in-store to your gross margin. I know it's kind of early on, but Ken, can you talk about how much of a penalty you've been incurring the last several quarters to Famous Footwear's gross margin from your online business? Just to kind of perhaps size the opportunity for gross margin improvement as buy-online-pickup-in-store gains momentum?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

Yes. Jeff. This is Ken. I mean, for every order that we're shipping, either from a store or from a warehouse on an online order, it's about a 15-point impact on just those shipping expenses to get it to the consumer. So if you go through and look at, it's basically $6 on your average unit retail. So, every time one of those customers elects to pick that up in the store, Rick and the team get the benefit of that difference. And so, on a mid-$40 AUR, it's pretty significant. So we've been very pleased with that and it also gives them an opportunity to engage with that customer when they come in as well.

Jeffrey Stein
Analyst, Northcoast Research Partners LLC

Q

Right. And Ken, any thoughts in terms of what percentage of your online orders now are being picked up in the store? Ken, recognizing it's early on.

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

Yes. It's early. That number – it's a double-digit number. So, we'll see where it all settles out. But right now, that's a double-digit percentage of the online orders.

Jeffrey Stein
Analyst, Northcoast Research Partners LLC

Q

Right. And last question real quick. Can you talk about the growth in your retail comps in your Brand Portfolio group? That is kind of a huge increase relative to what we've see historically. Maybe talk about what's going on there.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

Well, Jeff, I'm happy to report that in our Naturalizer stores, we saw comps, positive comps every month of this quarter, and the – probably starting the low single up to the mid single-digit range. We think that that had a tremendous amount – the impact on that was really through our speed-to-market programs where we could read and react and address very quickly. It allowed our teams to really bring in goods that were selling and move things quickly that weren't selling as well.

In addition to that, we had launched a new sport program for Naturalizer, so a combination of all the things I've been talking about for a while, plus the speed project, plus the sport aspect of it allowed it to perform as well.

Our Sam Edelman business, those comps were also up very, very strongly in the quarter. That has been up for a couple of reasons, I think it's just the power of how well Sam and his team are doing in terms of the right trends and getting that right is really number one. I think the second thing is we've begun to add different accessories into the mix of the stores, that's helped a little bit.

And I would say more important has really been the investments that we made and – in digital campaign as well as the inventory investment that we made for Sam in the first half of the year as well. So again, a combination of a number of factors that I think helped drive both of those things.

Jeffrey Stein
Analyst, Northcoast Research Partners LLC Q

Great. Thank you very much.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc. A

Yes.

Operator: And our next question is from the line of Laurent Vasilescu. Laurent, your line is open.

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

Thank you. Good afternoon. Congrats on solid results. I wanted to follow up on the Lifestyle Athletic number or the percentage rate, it grew up 20%, that's pretty impressive. Can you remind us what brands fall into that bucket? Any additional color on what's driving this growth?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc. A

It's not about brands, it's about the products themselves. So, we split our business into what we call performance side, which would be more product that's more specific to an activity, right – running, cross-training that kind of product versus the lifestyle business which we would consider court or lifestyle kind of product. So, the best example is Nike Tanjun is in the lifestyle product. Nike Flex is in the performance side. So they might both be – look like running shoes. One is more – has more properties of a running shoe, the other one is more about lifestyle. So that's – and Skate would be a lifestyle – all the Skate product would be a lifestyle business. Converse would be a lifestyle business.

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

Okay. That's very helpful. And then I wanted to follow up on the [ph] chance (32:55) of earnings between 3Q and 4Q. Can you remind us if there was any or were there any onetime items in last year's 4Q SG&A as we factor in the guidance on 3Q versus 4Q earnings?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc. A

No, not particularly. And I think that one of the reasons that we had tried to provide a little bit more back half color is with the acquisition, obviously, Allen Edmonds is a big fourth quarter business. I think as we work to diversify our brands and the brand portfolio, we get much more contribution there in the fourth quarter. And so, we try to help by sharing our third quarter expectations. We were up roughly 4% in the second quarter and would expect to be up roughly 4% in the third, so.

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

Okay. Very helpful. And any – and because Allen Edmonds is a bigger business in the fourth quarter, should we [ph] think that (33:56) the gross margins higher in the fourth quarter?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

The Allen Edmonds gross margin or the...

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

Q

The overall gross margin because of the contribution of Allen Edmonds.

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

Yeah. Well, it's not – I mean the margin I think has been pretty consistent throughout the last several quarters. So it's really more about the top line driving leverage.

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

Q

Okay. Very helpful. And then one more question. Kid's up high-single digits. Is that driven – I'm guessing that's driven by Skechers?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

It's driven by the same thing that's driving adults. So, it would be the Lifestyle Athletic product primarily that I described earlier.

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

Q

Okay. And then your last question. In terms of capital allocation, you paid down your revolver this year. Can we see additional share repurchase increase in dividend or could we see another tuck-in acquisition like Allen Edmonds to complement the existing portfolio?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

Yes. I mean, I think we're going to continue to pay our dividend, and certainly, we have been very happy with the success of the acquisition and the integration of Allen Edmonds. And so, for the right opportunity, we would be willing to allocate some more capital in that area.

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

Q

Okay. Thank you very much. Best of luck.

Operator: And our next question is from the line of Scott Krasik. Scott, your line is open.

Matt Gulmi
Analyst, The Buckingham Research Group, Inc.
Q

Hey, guys. This is Matt Gulmi on for Scott. Just wanted to revert back quick to commentary around back-to-school. You guys had mentioned that it was trending at plus low single digits. I was just wondering what your expectations were for the season and then is that kind of based on the growth that you're seeing within athletic as well that's accelerating the back-to-school sales?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.
A

The answer, the low single digit was our expectation for the time period, so we're pretty much right there. And, yes, athletic is still the accelerator for the business during back-to-school.

Matt Gulmi
Analyst, The Buckingham Research Group, Inc.
Q

Okay. And then, on the Allen Edmonds front, now that we're closer to 2018, have you guys kind of changed the way you think about it for next year and going forward? What's the right growth rate for that business?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.
A

No, I mean, we'll provide guidance for 2018 when we close out the year.

Matt Gulmi
Analyst, The Buckingham Research Group, Inc.
Q

Okay. Thanks, Ken.

Operator: And our next question is from the line of Steve Marotta. Steve, your line is open.

Steven L. Marotta
Analyst, C.L. King & Associates, Inc.
Q

Good afternoon, everybody. Can you please – congratulations also on a great quarter. Can you talk a little bit about Nike selling direct to Amazon and how you think that may affect your business in the short and longer term?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.
A

Well, I mean, I think there's – the good side of that business I think is it takes – cleans up the marketplace. I suppose it is one of the reasons that they were interested in doing it. I think until we see how it all rolls out and what that looks like, it hasn't – I haven't seen it do anything yet. But I think that remains to be seen, Steve. And then we'll do what we always do, we'll try to look at whether we need to change our assortment or adjust our assortment if there's something that's impacting it. But so far, I don't know how that's going to work until we see how it impacts and what the customer thinks.

Steven L. Marotta
Analyst, C.L. King & Associates, Inc.
Q

Okay. Without giving specific guidance [ph] across for (37:27) 2018, can you comment at all about how you feel open-to-buy dollars are being allocated by the wholesale channel for spring of 2018 and if that's up, down or relatively flat with last year?

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

Steve, it's Diane. I would say everyone is trying to do more with less, and that continues. So, our ability to replenish, to drop ship, to run our speed programs, to operate much more in real time is really going to be our answer to that. So, that's how we see us gaining share in the marketplace.

So, it's probably not going to be substantially different. There are maybe shifts between categories of businesses and brands based on their performance, but in total, we still see that everyone wanting to do more with less and chase goods as much as possible.

Steven L. Marotta
Analyst, C.L. King & Associates, Inc.

Q

Great. That's helpful. And, Ken, sorry if I missed it, interest expense expectations for the current year, please?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

Did we call that out, maybe...

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

No, we didn't but...

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

I mean, it's trending down. I think it was $4.4 million in the quarter. So, that was coming down, so you should be able to look at the last two quarters and then watch it decline. $35 million left on the revolver.

Steven L. Marotta
Analyst, C.L. King & Associates, Inc.

Q

Okay. Terrific. Thank you.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

Thank you.

Operator: And our next question is from the line of Chris Svezia. Chris, your line is open.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Good afternoon. Congratulations on the good quarter. So, I guess, first, on Famous. I guess, how important is – I guess, [ph] Audi (39:19) falls into the "Lifestyle" category, is that fair? And I guess that was a big or [ph] a high portion (39:29) contributor to the comp.

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.

A

That is – high portion of that business is – there's a few things in performance, but most of it is in Lifestyle.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay. And as you think about, Rick, there was a comment about SG&A leverage for Famous into the back half of the year, you're closing 70 stores. I think the occupancy cost is an SG&A, is that pretty much even between Q3 and Q4? You expect to get that leverage as a result of that?

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.

A

Yes. Yes. Obviously, we felt like it was wise to keep those stores open during back-to-school, our peak time, so that we start looking at closing them some time towards the end of September and through October depending on lease agreements. Some of them may be a little than that, maybe in January, but the bulk of them, I believe, will be closed before Christmas for sure.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay. Okay. And then how you specifically did, I guess, a pretty good job planning sandals, managing the inventory commitment there. How are you thinking about the boot business, fashion boot, functional boots, as you go into the back half of the year? How are you planning it for Famous? And I guess also, Diane, how are you thinking about that on the wholesale side?

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.

A

So, the biggest shift – I think we're planning, the total dollars are planned probably pretty close between when we say boots, so that's between cold weather, shearling, tall-shaft boots, and booties, but the categories themselves have had pretty substantial change. So, we have the booty categories being impacted higher, so we have more of those in part of our assortment, less on tall-shaft, and somewhat less on both shearling and cold weather.

So, but all in all, I think we're pretty flat. And the answer to what we expect is we expect flat and that's what we'll manage our business to, but this will all depend on what price points we sell everything at. So if we can sell it earlier and when weather changes or the trends are correct, we can do a little better, if not, we'll do a little worse. But I think that's about where we thought it be, it'd be in the grand scheme of things, is about flat.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

Yeah, I would say...

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

...that Chris, that's pretty consistent with the Brand Portfolio, that's pretty much how people planned it. One of the things that you can see if you're in the market today that a lot of the newness has really been moved from August to September. So, there's not as much out there right now. But what is out there is selling really nicely, particularly in the short boot category and you were seeing a little bit more on, with embroidery and Western-influenced look seem to be doing well early on and actually a little bit more on the dress side now for a change of pace. But early to tell yet, big delivery coming up the end of this month and into early September.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay. Ken, question for you on gross margin. I'm just curious, you've done 100-basis-point-plus in the first half. Your guidance is, call it, 50-ish on average or thereabouts for the year. Obviously, Allen Edmonds added as a piece to it the inventory management component, I mean, it seems like you still expect pretty consistent gross margin improvement, but your guidance assumes a inflection in the back half even as Allen Edmonds becomes a bigger piece of the business. So, kind of walk through why that would potentially be the case.

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

Well, I think clearly, we've been trending a little bit higher than our guidance. So, I think just watching what's happening in the marketplace and wanting to make sure that we maintain our flexibility, we're also – we're going in, Malcolm has come in. He's looking at a lot of how we're going to be going to market with the Allen Edmonds business.

And so, I think that excluding Allen Edmonds, I think we're still feeling pretty good about where that guidance range is. And I think the wildcard is what kind of response we ultimately end up doing there as we look at our pricing and promotional cadence with that business. So, we're running a little better than that. And I think that there's probably a little bit of upside there.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Okay. Thank you. Final question, Diane, just as you think about Allen Edmonds and how well that has gone for you, how do you think about the acquisition profile of the company? Are you more [ph] set to it (43:41), no change, balance sheets improving, seems like you can have dry powder to do something sooner rather than later? I'm just curious about your thought process there. Thank you.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

Yes. No, I've obviously been very pleased with the way the teams have handled this integration and we're excited, still remain the same – as excited as we were about the prospects for that brand going forward. So, I'd have to say that I continue to have the same amount of excitement as I've had up to this point in time. But with a really higher degree of confidence about our team's ability to integrate these brands and to drive, make sure they are creative and a benefit for shareholders. So, I'm definitely in the motive of looking for the right brand that fits with our portfolio well, so very open to it.

Christopher Svezia
Analyst, Wedbush Securities, Inc.

Q

Sounds good. All the best. Thank you very much.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

Thank you.

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.

A

Thanks, Chris.

Operator: And our next question is from Jeff Stein. Jeff, your line is open.

Jeffrey Stein
Analyst, Northcoast Research Partners LLC

Q

Yes. Just one quick follow-up question for Ken. Ken, if you look at your SG&A just for your Brand Portfolio group, it was up almost 40% in the second quarter. So I'm wondering can you tell us what the organic SG&A percentage was for that group excluding Allen Edmonds?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

Yes. If you look at that, it had, I think, we said in our prepared remarks $20 million of expense roughly associated with Allen Edmonds. So, you take that reported number and just back out the $20 million, there was, I think 6.8% is what we said.

Jeffrey Stein
Analyst, Northcoast Research Partners LLC

Q

Perfect. Okay. Sorry, I missed that. Thank you.

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

Yes.

Operator: And our next question is from the line of Sam Poser. Sam, your line is open.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

Good afternoon, everybody. I have a few questions. What is the exact share count for the quarter that was on the press release? Just sort of housekeeping...

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

$43 million, I think? I'm pulling the exact number for you.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

While you're digging around, in the quarter, you had your EBIT margin increase? It was down in Q1; it was up in Q2 and you're really telling us it's going to be down again in Q3 just based on sort of what you're telling us as far as the growth. Can you tell us sort of how you're looking at that and why that's the case while you're digging that out?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

So let me give you the share count here so that you have that. So for the quarter, the – so we have the dilutive effective number was 41,954.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

Thank you.

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

All right. And what was your other question, Sam, on the...

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

The question is in Q3, you're basically implying that your EBIT margin is going to be down after being up this quarter. What changed – and then up again in the fourth quarter. What change are you seeing that makes the EBIT margin down? I mean if you're saying the growth is going to be at around 4% again in the EPS, then that's implying that your EBIT margin is going to be down slightly?

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

Yes. And so, that is a – the weighting is much higher to Famous in the third quarter. And so, typically that third quarter margin and gross profit in Famous is always lower in the third quarter than it is in the second quarter. That's the biggest contributor.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

Well, that was true last year too. And last year in the third quarter, Famous' gross margin was down 111 bps, and it was down 43 bps the year before. So, what's going – why isn't that correcting itself? It was – Q2, you're up against a plus 13 bps and a plus 57 bps. So, why would this continue to be down on top of relatively easy comparisons versus being down after the little more difficult comparisons in Q2?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

Yes, I think it has to do with the ratio of the growth. There's a larger growth of that in the third quarter.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

Okay. So...

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

We're expecting the rate, the EBIT rate at Famous to be higher in the third quarter year-over-year, but it's really the mix impact of the third quarter.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

...okay. All right. And then could you just give us the exact dollars for that – you'll put it in the Q, but the exact dollars for Healthy Living and for your Contemporary Fashion businesses?

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

It's in the slide, but I can look for you.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

Sure.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

For Healthy Living, sales were $125 million, down 1.9%. Contemporary Fashion sales of $146.8 million were up 39.7%.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

And the – $125 million to $146.8 million and that $146.8 million includes $41 million of – $41.8 million of Allen Edmonds, correct?

Kenneth H. Hannah
Chief Financial Officer & Senior Vice President, Caleres, Inc.

A

Correct.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

Yes.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

All right. Well, thank you, guys and continued success.

Richard M. Ausick
Division President, Famous Footwear, Caleres, Inc.

A

Thank you, Sam.

Sam Poser
Analyst, Susquehanna Financial Group LLLP

Q

You're welcome, thanks.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

A

Thanks, Sam. Appreciate it.

Operator: And at this time, we have no further audio questions. Presenters, I turn it back to you for closing comments.

Diane M. Sullivan
Chairman, President & Chief Executive Officer, Caleres, Inc.

All right. Thank you, Ian. Thanks, everyone, for joining us. Again, sending all good wishes out to everybody in Houston and hoping that rain stops soon. Take care.

Operator: Ladies and gentlemen, this does conclude today's conference call. We thank you greatly for your participation today. You may now disconnect.