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JWN - Q1 2019 Nordstrom Inc Earnings Call

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OVERVIEW:

Co. reported 1Q19 results. Expects 2019 EPS to be $3.25-3.65.

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PRESENTATION

Operator

Greetings, and welcome to the Nordstrom First Quarter Earnings Conference Call. (Operator Instructions) As a reminder, this conference is being recorded.

At this time, I'll turn the call over to Trina Schurman, Director of Investor Relations for Nordstrom. You may begin.

Trina Schurman *- Nordstrom, Inc. - Director of IR*

Good afternoon, and thank you for joining us. Today's earnings call will last 45 minutes and will include 30 minutes for your questions.

Before we begin, I want to mention that we'll be referring to slides, which can be viewed by going to the Investor Relations section on nordstrom.com.

Our discussion may include forward-looking statements, so please refer to the slide showing our safe harbor language.

Participating in today's call are Erik Nordstrom, Co-President; and Anne Bramman, Chief Financial Officer, who will discuss the company's first quarter performance and outlook for 2019. Joining during the Q&A session will be Pete Nordstrom, Co-President.

With that, I'll turn the call over to Erik.

Erik B. Nordstrom - *Nordstrom, Inc. - Co-President, Principal Executive Officer & Director*

Thank you for joining us today. While we believe our customer strategy and business model position us for long-term success, our first quarter top line results were well below our expectations. We had planned for a continuation of soft sales trends from the fourth quarter but saw further deceleration. Relative to the plans we shared at the beginning of the year, we successfully executed on inventory and expense, which helped mitigate our sales mix. We ended the quarter with inventories in solid shape, and our financial position remains strong. We're confident in our leadership team's ability to better serve customers on their terms and remain focused on achieving profitable growth.

During the first quarter, we had some executional misses with the customer experience that had an impact on sales across Full-Price and Off-Price both in stores and online. We know we disappointed our customers, and we own it. We have identified 3 factors that contributed to this sales miss: loyalty, digital marketing, and merchandise. These areas are within our control to turn around, and we're already taking steps to course correct and drive the top line. I'd like to provide insight into what happened and how we're addressing all 3 areas.

Beginning with loyalty. We have a well-established program with nearly 12 million active customers contributing more than 60% of sales in the first quarter. Last fall, we evolved the program with the introduction of The Nordy Club, which allows customers to earn reward notes faster and provides early access to product and events. However, the execution of our rollout was not as successful as we had planned. As part of our decision to move to a digital-first program, we eliminated paper notes but later discovered that a segment of our customer base relies on receiving these notes by mail. As a result, we saw a reduction in traffic across Full-Price and Off-Price. We are resolving these issues, and our initial results showed improving trends for engagement, traffic and spend from our loyalty customers.

The second factor is related to digital marketing. We deliberately reduced our digital marketing as we shifted resources to loyalty. With The Nordy Club rollout not ramping as we had projected, we experienced incremental traffic declines in our business. We have since increased our investments in digital marketing to drive traffic and sales.

The third factor is merchandise. The breadth of our offering across brands, price points and styles is a key differentiator in serving customers. We have opportunities to rebalance our assortment mix to better resonate with customers in Full-Price and Off-Price. This includes Women's Apparel, which continued to have the toughest results in Full-Price. Beauty was another call out for the quarter given the highly promotional environment and increased out-of-stock levels. It will take some time to adjust our merchandise assortment, but we have already started this process and expect improvement in the second half of the year.

All 3 factors, loyalty, digital marketing and merchandise, contributed to a slowdown in digital sales growth of 7% in the first quarter relative to last year's annual growth of 16%. We're making the changes we believe are necessary to drive our top line as we continue our aggressive focus on expenses, which Anne will discuss in more detail.

Our strength is our commitment to the customer, and we know we have areas for improvement. Over the years, we have managed through many cycles, which give us confidence in our ability to adjust our business to better serve customers. Our entire leadership team has a high degree of urgency to improve our top line and profitability. Additionally, the team is focused on executing the following three key strategies this year. First, our local market strategy enables increased customer engagement through services and greater access to merchandise selection with faster delivery and at a lower cost to us. Last year, we launched in Los Angeles our largest market with four full-line stores and three Nordstrom Local service hubs. During the first quarter, we continued to see positive outcomes with outsized growth in digital sales and store traffic in this market. In addition, nearly 1/3 of order pickup services are done in our three Nordstrom Locals. We're planning to scale in the L.A. market, including 16 full-line stores by further leveraging inventory through our supply chain investments.

Moving to our second key strategy. Our market share gains in Los Angeles give us added confidence as we expand our presence in New York City, our largest market for online sales. We are on track to open our flagship on October 24 along with two Nordstrom Local hubs this fall. We expect these physical assets to greatly add to our ability to engage with customers across multiple touch points. We know that engaged customers spend more, which is expected to result in a meaningful sales lift for this important market.

With our third strategy, we're focused on improving the customer experience during our two key events. Our Anniversary Sale is a unique event, offering brand-new arrivals at reduced prices for a limited time. We're curating our assortment to focus on customers' favorite brands. We're also extending the preshop period for our top loyalty customers.

For holiday, we're aiming to make Nordstrom more of a gift-giving destination for both new and existing customers. This includes amplifying our gifting assortment across categories and with more accessible price points.

In closing, we own our result, and we're focused on getting our sales back on track. As always, the customer is at the center of everything we do, and through that lens, we're committed to better serving them on their terms.

Now Anne will discuss our financial results and outlook.

Anne L. Bramman - *Nordstrom, Inc. - CFO*

Thank you, Erik. I'd like to reiterate that we take an immediate action to better serve our customers for our top line and improve profitability. As we continue to focus on making our business more efficient and productive, we're aggressively bending the expense curve and managing our inventory.

Turning to our top line results. Total company sales were down 3.5% with Full-Price down 5.1% and Off-Price down 0.6%. The drivers of our sales shortfall - loyalty, digital marketing and merchandise - contributed to decelerating trends in our key operating metrics, which includes trips and customer engagement.

Although we missed our sales expectations by several hundred basis points, we were able to offset roughly half of this miss through our merchandise margins and expense performance. In fact, the sales shortfall in Off-Price was fully offset by the team's ability to control expenses and manage inventory levels down significantly.

Moving to gross profit. Our rate was down 60 basis points relative to last year due to planned markdowns and occupancy deleverage. We ended the quarter in a solid inventory position with a positive spread of 180 basis points relative to sales. This allows us to be agile in responding to changes in customer expectations. As we continue into the second quarter, we have planned inventory based on current sales trends, and we remain disciplined in our buys as we work to improve our merchandise offering.

From an expense standpoint, our SG&A rate increased 168 basis points relative to last year. This was entirely due to fixed cost deleverage on lower sales. We're making further structural enhancements to our operating model as we implement several efficiency initiatives related to three areas: improvements to our store operating model, productivity gains in technology and supply chain and reduced discretionary spend. We expect these initiatives to ramp up over the year, and we're ahead of our plans with $35 million realized in the first quarter. This included operational changes in stores to better align with how customers are shopping. For example, for improving services that have a direct customer impact such as order fulfillment in full-line stores and faster checkout at the Rack. All these initiatives represent permanent reductions in our cost structure, which positions us well for strong EBIT flow-through going forward.

Another lever of improved profitability is our generational investments. Over the past decade, we've invested early in our digital capabilities and new markets. This is the last year of our generational investment cycle, and we're already seeing returns. These investments are continuing to scale and are expected to deliver top line growth and improved profitability this year.

Our financial position remains strong, enabling us to be flexible in changing business conditions. We have a healthy balance sheet and generating annual operating cash flow of more than $1 billion over the last decade. Our consistent and balanced capital allocation approach enables us to maintain an investment-grade credit rating. We also returned approximately $250 million to shareholders through dividends and share repurchases during the first quarter.

Moving to our annual outlook. We revised EPS from a range of $3.65 to $3.90 to a range of $3.25 to $3.65. This incorporates a sales decline of 2% to flat growth for the year relative to our prior outlook of 1% to 2% increase. We expect it's going to take some time to see improvement as we further adjust our merchandise offerings and lap the operational issues from the Nordy Club rollout.

We anticipate first quarter trends to continue into the second quarter with gradual improvement beginning in the second half of the year. For credit revenue, we're planning for a low to mid-single-digit increase based on our current sales trends.

From a bottom line perspective, we expect an EBIT margin range of 5.3% to 5.8% compared to our prior outlook of 5.9% to 6.1%. From a gross profit and SG&A perspective, the change in our assumptions is driven by greater fixed cost deleverage and lower sales expectations. We expect gross profit at the midpoint of our outlook to be relatively flat to last year. This reflects improved merchandise margins offset by occupancy deleverage.

For SG&A, we expect moderate deleverage when excluding the estimated credit charge in 2018. We've also incorporated expense savings at the high end of our original range of $150 million to $200 million. These savings are expected to be back-half weighted as we make further progress on our various initiatives.

For the second quarter, we expect our anniversary event to perform in line with our current sales trends, which has been our historical experience. Our second quarter gross profit rate deleverage is planned similar to Q1 due to lower sales. We also expect SG&A to deleverage but to a lesser extent than Q1 due to further expense savings.

Specific to Anniversary, we're making changes to improve the overall economics of the event. As a result, we expect extended merchandise margins in the third quarter for better sell-through at the Anniversary product, which should result in lower markdowns. Please also refer to our slides for additional color on our quarterly timing assumptions.

In closing, we're making hard choices as we focus on better serving customers, driving top line and improving profitability. We know we must demonstrate this commitment with our results in the coming months, and we look forward to updating you on our progress.

I'll now turn it over to Trina for Q&A.

Trina Schurman - *Nordstrom, Inc. - Director of IR*

Thank you, Anne. (Operator Instructions)

We'll now move to the Q&A session.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Our first question is from the line of Ed Yruma with KeyBanc Capital Markets.

Edward James Yruma - *KeyBanc Capital Markets Inc., Research Division - MD & Senior Research Analyst*

Thanks for giving the diagnostic on the issues you suffered during the quarter. I guess if you could click down a little bit and maybe talk more specifically about Rack. It seems like a lot of what you spoke about was related to the e-com business and the full-line. And as you look at Rack, kind of how should we think of that progression improving through the course of the year?

Erik B. Nordstrom - *Nordstrom, Inc. - Co-President, Principal Executive Officer & Director*

Ed, this is Erik. I'll take that one. Well, first of all, we'll start with the subject we touched on kind of across Full-Price and Off-Price. So the notes, digital marketing certainly affected our Off-Price business as well both in-store and online. We also have merchandise mix issues to get after within Off-Price as well. When you get into the details, Off-Price is a little different than Full-Price. There are some variance department by department. But that mix, and you know us well, that mix is so vital, that mix we have across Off-Price to Full-Price, that mix of price points that we have, the mix of styles. We have a pretty broad range of customers that we look to serve, and our merchandise mix is super important in delivering that. And when we get out of balance, it really affects our top line. So we have those issues in Off-Price.

The other bucket I'd call out is we did enter the year with a plan to improve our profitability in Off-Price, and part of that plan was eliminating some unprofitable events. Specifically, we reduced the number of flash events that we had on HauteLook. Some of those were not profitable. We reduced our Clear the Racks event in the quarter. And we did eliminate some of the very lowest price points merchandise we had on our Off-Price e-Commerce business. We did get the profitability improvement from those decisions. The effect on top line was greater than we had planned. And we look at that, and we see opportunities to not blow up that strategy but to make some adjustments to it that we can and will help our top line.

Operator

Next is Alexandra Walvis with Goldman Sachs.

Alexandra E. Walvis - *Goldman Sachs Group Inc., Research Division - Research Analyst*

You outlined the drivers of the change to the guidance for this full year. I wonder, as we reflect on the last couple of quarters, whether you're thinking any differently at this stage about some of the long-term guidance that you gave at the Investor Day from last year or even the trajectory to move towards that.

Anne L. Bramman - *Nordstrom, Inc. - CFO*

Alex, this is Anne. So on the long-term profitability target, yes, at this stage, we have a lot of the year left to deliver. So about 70% of year left to deliver as we talked about the path that we gave in the Investor Day financial goals. We're playing that out a little bit differently. So we can talk a little bit about the growth profit levers that we were pulling there. We're proceeding on those and we're getting the terms that we need but we're also accelerating the expense savings productivity on that, making structural changes on that.

So the good news is, is once we get the top line back on course, the flow-through should actually be greater than what we had signaled in the Investor Day. So right now, we just want to play out the rest of the year, get back on track with the initiatives we talked about and then see where we land in the year before we update anything.

Operator

Next is Mark Altschwager with Robert W. Baird.

Mark R. Altschwager - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Just following up on the earlier comments about taking some steps to drive the profit improvement at Rack. I'm wondering, on the slide where you show the generational investments detail, it looks like you've reduced your profit expectations for the Rack.com, Trunk Club Canada bucket. Could you just talk a little bit about that? I mean presumably that's some of the sales reduction that you're seeing. But just any other clarity on how you're looking at kind of the profit contribution from that generational investment and sort of what the path should look like over the course of the next 1 to 2 years?

Anne L. Bramman - *Nordstrom, Inc. - CFO*

Hi Mark, yes. You're right. We did take slightly down the top line and the profit improvement piece to it, and it's really about NRHL, Trunk Club, the current businesses. And it's just in line with the sales decline that we've seen in general for the quarter and what we'll even guide on for the year. There's nothing else structurally different with that. It's just once we get -- again we pull this lever, we can get back on track, we should see better flow-through coming through on that.

Operator

Next is Paul Trussell with Deutsche Bank.

Paul Trussell - *Deutsche Bank AG, Research Division - Research Analyst*

Also referring to the slide deck, you give some assistance with timing of assumptions. And just wanted to inquire about some of the second half comments that you make. If you could just maybe walk us through how we should think about the impact of the NYC opening to revenues. What are the drivers behind the second half merchandise margin expansion? And then anything else just to be mindful of as it relates to second half versus first half?

Anne L. Bramman - *Nordstrom, Inc. - CFO*

Yes. So I'll give some high-level commentary on it, as you mentioned, we really did try to expand out the assumptions that we've been giving -- that we're giving you first half, second half when the quarter plays out. So for detailed model questions, I would just refer you to Trina for after the earnings call.

But just stepping back and looking at the high-level story. So we would expect to see some gradual improvement that really more towards the back half of second half of the year on the top line component to it. New York is a piece of it as far as the tower opening and entering that market with our local market strategy. But really, the pieces that we're seeing coming through in -- on the EBIT side is really getting more benefit out of the expecting initiative we've got with SG&A and continuing to hold the strategy we have on our merch margins, primarily with Anniversary that I talked about in my opening comments, having a higher sell-through should help particularly in Q3. And then as we exit out the year, we would expect to see the flow-through from that as well as the SG&A savings.

Operator

Next is Matthew Boss with JPMorgan.

Matthew Robert Boss - *JP Morgan Chase & Co, Research Division - MD and Senior Analyst*

At Full-Price, I guess as you dissect the softness that you're currently seeing in Women's Apparel and the Beauty category, how are you thinking about the timing for improvement? Do you think the issue is differentiation of the merchandise? Or is it more value proposition and, like you talked about, some more entry-level price points? And I guess just near term, what are the actions you're taking to stabilize these two businesses?

Peter E. Nordstrom - *Nordstrom, Inc. - Co-President & Director*

Yes. This is Pete. I would -- they're different. With Beauty, we have some things that happen to us that they're relatively discrete, I think, in nature. We had some out-of-stock issues that was a result of just being in stock, really getting us some of the vendor -- our vendor partners there. There were some issues there that we think will mostly be behind us here pretty quick. We also had a lot of price promotion issues in Beauty, and that caused some problems with it. But I think Beauty has been such a consistently good performer for us over the years if you kind of look at that track record. We expect that, that will get back on track pretty quickly.

With Women's Apparel, we have some more broad-based issues. A lot of it has to do with the balanced price that Erik talked a little bit about. I think in particular, finding ways to appeal more to young customers kind of in the range of what we do there in Women's Apparel. I think we know what we need to do there. And the good news is that part of the business turns relatively quickly. But I think in terms of really being able to make the changes we feel like we need to make, that's going to take a few months.

So I think on the whole, Women's Apparel and Beauty is a subset of all. But I think it's fair to say that more broadly, we definitely have an opportunity to be better connected with customers in terms of the relevance that we have to offer, and the balance of price was probably the biggest lever there.

Operator

Next is Simeon Siegel with Nomura.

Simeon Avram Siegel - *Nomura Securities Co. Ltd., Research Division - Executive Director & Senior Analyst*

Anne, could you just remind us what percent of your expense structure is fixed versus variable now? Just recognizing the deleverage from the lower sales, I thought you had a pretty variable expense model. So any thoughts or help there? And then just any way to quantify maybe on a full year basis what each point of comp pressure does to the annual margin?

Anne L. Bramman - *Nordstrom, Inc. - CFO*

Yes. I don't think we've given the explicit details between fixed and variable. But what I can say is in the Full-Price business in particular is much more of a variable model than our Off-Price business given the commission structure for our sales force in the stores. Having said that, as far as the comp piece to it, I think what you -- our sales growth structure, I think what you can see from even from Q1, and for how we're giving guidance for the year, is that we're actually shifting that a bit. So if you think through our midpoint, which is down 1%, the flow-through actually is a little bit better given the fact that we are holding the strategy on our gross margin as well as SG&A.

So I think if you do the reversed logistics on that, you can see that it's -- over time, as we make these structural changes, you would need less of a top line growth, and we're seeing that flow through.

Operator

Next is Chuck Grom with Gordon Haskett.

Charles P. Grom - *Gordon Haskett Research Advisors - MD & Senior Analyst of Retail*

I'm just trying to reconcile your comments about taking some time to fix some of the issues on the merchandise side of the issues here for you guys with your comp, the implied acceleration on the 2-year stack. So maybe just help us walk through how it's going to improve both on the full-line and then also on the Rack.

Anne L. Bramman - *Nordstrom, Inc. - CFO*

So I think -- let me just frame up a little bit as far as the guidance we've given. So when you look at the weighting between first half and second half, we're not off that significantly based if you could just look at the top line sales growth or the top line sales guidance that we've given between first half and second half is not all that off what you've seen historically. The only change is the fact that you've got the New York market opening up in Q4, which is slightly higher for the second half lift in top line.

So when we look at the overall stack, what we're assuming is that it's going to take a few months to get back on track on the assortment side. And the good news is our inventory position is in a very good place. We got a couple pockets that are still coming through. But exiting out of the quarter allows us to be very agile, and reactive as we start rebalancing the assortment to get back to what we need to. That's the great news on that and then the expense productivity that we've got is allowing us to mitigate some of the top line issues.

Operator

Next is Kimberly Greenberger with Morgan Stanley.

Kimberly Conroy Greenberger - *Morgan Stanley, Research Division - MD*

Anne, you talked about making SG&A more efficient. I'm just wondering if the company has considered making more aggressive cost cuts across the organization. And if not, do you think there are areas that are opportunities or represent opportunities for that kind of initiative?

Anne L. Bramman - *Nordstrom, Inc. - CFO*

Yes. Kimberly, so when I talk about the savings that we're going after, we're actually ahead of our plans and we'll be at the higher end of the $200 million we planned that's better than what we shared at the Investor Day last year. Let me put those in 3 broad buckets that we're going after.

First is productivity, end-to-end productivity primarily, technological and supply chain. So those are some very big structural pieces. It takes some time to work through those. But those are some big buckets that we're going after from a productivity perspective.

The second piece we've already implemented, which is store operating model changes I talked about in my opening comments. And that was a piece -- it actually gets us back in line with what the customer wants but also helps drive the expense efficiency in the stores as well.

And then I think the smaller bucket I would talk about is the discretionary spend. It's really not that -- it's the smallest component of what we're looking at in the cost savings that we have. And so that's how I would frame that up. Now what I would also say is that we're continuing to look for opportunities to drive more productivity end to end in the business.

And so you know us. We will continue to invest in doing the right thing for the customer, and we'll continue to invest in this business. But we're also going to look at how we make sure that our expense structure stays in line with whatever trends we see in our top line.

Operator

Next is Paul Lejuez with Citi.

Paul Lawrence Lejuez - *Citigroup Inc, Research Division - MD and Senior Analyst*

Just a follow-up on the last question and one other. Do you think there's anything that you might have cut back on from an SG&A perspective that might be negatively impacting the top line either in the Full-Price business or the Rack business? And then just separately, curious about the reduction on the credit line if that is simply a reflection of lower sales expectations or if there's something going on in the credit portfolio that you can share with us.

Anne L. Bramman - *Nordstrom, Inc. - CFO*

Hi Paul, so I'll start with the cuts component to it. And I don't know if, Erik, if you want to chime in as well and I can give you more color on credit.

So when we look at the SG&A component to it, I think we'll see if it's really driving more efficiency, and we don't believe it's impacting the top line. And we talked about the drivers of the top line was really about some of the executional opportunities we had with Nordy Club, some of the digital marketing components as well as the assortment. We have gotten back into the marketing component, which is baked into our SG&A line. So you can see, we're offsetting that.

And then on the credit side, we have talked about this in the last call, as you recall, that we are anniversary-ing a credit acquisition or customer acquisition event from last year. We'll finish anniversary-ing that in second quarter. And then when you look at the guidance for the year, it's really commensurate with what we're seeing with the sales trends. So nothing else in particular about credit. I don't know if, Erik...

Erik B. Nordstrom - *Nordstrom, Inc. - Co-President, Principal Executive Officer & Director*

Yes. I'll add a little color on that. With loyalty and marketing, our missteps were not motivated by cutting expenses. We actually invested in our loyalty program. We upped the points from two points for every dollar spent to three points. We added a number of experiences to the program, which are actually resonating really well with the customers. But in having the executional issues around the notes directly affected our digital marketing plan. By investing in loyalty, we moved marketing dollars there and away from retention and activation in our digital marketing. So our missteps with the loyalty program exacerbated our issues in digital marketing, and they're certainly connected but again not driven by expense.

Another thing I'd call out is in our stores, both in Racks and in our full-line stores, we have executed some model changes at our stores, again, not driven mainly by expense. But we've been on this journey for a while of, clearly, our model needs to change. Our business model, which is born in bricks-and-mortar stores, and define what the role of stores are. We think we have real good clarity on that. Our stores still that role of having great sales people who are taking care of one customer at a time and making some genuine human connections. That's in our DNA. That's continuing -- it has to be important.

But increasingly, stores play a fulfillment role. They're locations where customers can pick up online orders, and they are locations that we fill online orders from. So we have moved our labor model in our stores to reflect what customers want and need. And there are efficiency opportunities in there. But I wouldn't say that it's been a blunt force of getting after expense cuts. I would say that, that's been done with, boy, how is the customers' needs changing, what are they looking for, how can we leverage the physical assets we have in stores and the people in our stores and the inventory in our stores to better serve them on their terms. And that's actually gone really well this quarter.

Operator

Next is Michael Binetti with Crédit Suisse.

Michael Charles Binetti - *Crédit Suisse AG, Research Division - Research Analyst*

So as I look at the -- I'm just looking at quick tactical question on the lease accounting. I know there are some changes in accounting, but it looks like it was in the ROIC calculation you guys give in the press release is significantly lower than last year, I think you report just over 200 versus 250 last year. I think that would be one of the positive contributors to the gross margin in the quarter. Just since it's down so much in that, I want to see if you can maybe help us think through how much that contributed to gross in the quarter. And is that kind of level that we'll see going forward under the new accounting? And then I had a quick follow-up.

Anne L. Bramman - *Nordstrom, Inc. - CFO*

Yes. So on the lease accounting, we actually have a disclosure in the press release and there's a supplemental, Trina can walk you through that. What I would say broadly is that it really had no material impact at all to our financials and even ROIC, it was less than a 1/10 of a point. So -- of the turn. So I think -- so Trina can walk you through but as far as overall balance sheet in the income statement, there's virtually no material impact at all.

Michael Charles Binetti - *Crédit Suisse AG, Research Division - Research Analyst*

Okay. So I guess I would just want to step back a minute and think a little bit bigger picture here. And You guys have given some good tactical thoughts on how you're approaching merchandising and loyalty and everything in light of the recent sales volatility. But if we look at Full-Price, the dollar level of that business is in the same place it was in 2014. And you guys have done a nice job of one of the premier dot-com businesses in the sector. Obviously, it's well known that brick-and-mortar department stores have had traffic challenges. But how do you think bigger picture about what you think the Full-Price business needs to become a bigger business that's back on track to higher revenue base as these current dynamics that we see in the marketplace continue to be headwinds going forward?

Erik B. Nordstrom - *Nordstrom, Inc. - Co-President, Principal Executive Officer & Director*

Yes. Michael, It's Erik. I'd like to take that. Specifically, we would point to our local market strategy. And let me be clear. That is our model for the future. We started in L.A. last year and really started with engagement. How do we engage with customers by leveraging both our digital and physical assets? And that included experimenting with new physical assets in the Nordstrom Local service hubs. That engagement part across services and across channels, and we know we've got a lot of data on that. We know the more we engage with customers across channels and services, the more they spend. That's gone really, really well.

The second part of the local market strategy is leveraging the inventory that is close to our customers, either in our stores or in our supply chain facilities. That's -- we're not as deep into that yet. We started being able to leverage the inventory. Started with our 4 core stores in Los Angeles. And a good example would be BOPUS, Buy Online, Pick Up in Store, where we went from the available inventory for BOPUS being one specific store's inventory to connecting the 4 stores and being able to pick it up either at those four stores or one of the three Nordstrom Local service hubs we have. And we talked about it before, the outsized growth we're seeing in BOPUS across our company. The growth in BOPUS in Los Angeles is about 2x that we're seeing elsewhere in the company.

So here is a massive piece of engagement that customers love, that we think we can do in a fairly unique way and really given our customers terms, that drives higher engagement, drives bigger spend. Ultimately, our local market strategy success metric is gaining market share in these markets, and we have seen that in Los Angeles. We're in the midst right now of expanding our local market services from those core four stores to all 16 full-line stores in Los Angeles. We are on pace to bring our learnings to New York when we open the tower. We have two Nordstrom Local service hubs planned on the island. And we're well positioned to execute that in New York. And our plan is next year to take that to our biggest markets across our portfolio.

So that is our model. It leads with service engagement across channels and services, and it leads with leveraging inventory to get customers a greater selection to them faster and at better economics for us. And we think that's the future of our Full-Price business.

Operator

Our last question comes from Priya Ohri-Gupta with Barclays.

Priya Joy Ohri-Gupta - *Barclays Bank PLC, Research Division - Director & Fixed Income Research Analyst*

In light of the revised guidance, it looks like you're still going to be outside of your targeted leverage range. I'm wondering if you could share with us any conversations you might have had with the rating agencies as to whether there might be any change in how they're looking at your current ratings or potentially the outlook that they have on those ratings.

Anne L. Bramman - *Nordstrom, Inc. - CFO*

Yes. So we remain very comfortable with our range, and we expect to be in line with our expectations or historical levels by the end of the year. And as you -- and we've talked about this a lot. We have a very consistent capital allocation approach. And so we remain committed to being an investment-grade company. And we look at our balance sheet. And so as we think about the guiding principles around capital allocation, that is a big piece of that.

Trina Schurman - *Nordstrom, Inc. - Director of IR*

Thank you for joining today's call. A replay along, with the slide presentation and prepared remarks, will be available for 1 year on our website. Thank you for your interest in Nordstrom.

Operator

This concludes today's teleconference. You may disconnect your lines at this time, and we thank you for your participation.
