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JWN - Q1 2018 Nordstrom Inc Earnings Call

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OVERVIEW:

Co. reported 1Q18 EPS of $0.51. Expects 2018 EPS to be $3.35-3.55.

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PRESENTATION

Operator

Greetings, and welcome to the Nordstrom First Quarter Earnings Conference Call. (Operator Instructions)

We will begin with prepared remarks, followed by a question-and-answer session. (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, Investor Relations*

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 could be viewed by going to nordstrom.com in the Investor Relations section.

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

During today's call, the company does not plan to comment further on the going private exploration process by the Nordstrom family.

Participating in today's call are Blake Nordstrom, Co-President; and Anne Bramman, Chief Financial Officer, who will discuss the company's first quarter performance and the outlook for 2018. Joining during the Q&A session will be Erik and Pete Nordstrom, Co-Presidents; and Jamie Nordstrom, President of Stores.

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

Blake W. Nordstrom - *Nordstrom, Inc. - Co-President & Director*

Good afternoon, and thank you for joining us. Our first quarter results reflected our ongoing efforts to integrate our digital and physical assets to serve customers in new and relevant ways.

Our overall sales performance was in line with our expectations. We delivered total sales growth of 5.8%. This included an increase of around 250 basis points, primarily from a loyalty event shift. Comp sales, which are reported on a like-for-like basis, increased 0.6%.

The investments we're making in digital continue to pay off. During the quarter, we generated an 18% increase in sales, enabled through our digital capabilities, compared to the previous year.

Our full-price comp sales increase of 0.7% was generally consistent with our trends. Our off-price comp sales increased 0.4%. While we're not satisfied with recent trends in our stores, we're focused on making improvements to our Rack business.

On April 12, we achieved a significant milestone in our company's history with the opening of our first ever full-line Men's Store in New York City located near Columbus Circle. This 3-level, 47,000-square-foot store features our latest service experiences to help serve customers on their terms, including express returns kiosk, same-day delivery, 24/7 buy online and pick up in store and unique brand partnerships.

Our Men's Store opened ahead of our New York City flagship, which is scheduled for fall of 2019, and we're off to a good start. Manhattan is a premier retail destination and represents our largest online market serving customers. Based on our experience of introducing full-line stores in new markets, we also expect this flagship to deliver a meaningful sales lift in New York City.

This quarter marked another important achievement with the introduction of Nordstrom Rack in Canada. Like our experience in the U.S., we expect synergies between our full-price and off-price businesses. We're seeing terrific results from our 3 store openings this spring in the Toronto and Calgary markets, with 3 more openings planned for this fall.

We continue to grow our strategic brand partnerships with a focus on establishing Nordstrom as the partner of choice for brands and providing customers with newness. We want to create a sense of discovery through these collaborations, while supporting our regular price sell-in. Our strategic brands include new and emerging partners, along with established ones.

During the time of transformation in the industry, we've been investing in digital capabilities to expand our customer reach and engagement. This uniquely positions us to increase market share and drive growth. Our customer-focused approach informs how we allocate capital with the goal of driving customer engagement, market share gains and improved profitability.

In our top markets, we're further integrating our digital and physical assets across supply chain, technology, marketing and merchandising to deliver differentiated services and experiences. To lead our efforts, we recently named Ken Worzel as our Chief Digital Officer. As one of our top leaders, Ken is instrumental in driving our digital strategy as we continue to evolve our business. He will also continue in his role as President of Nordstrom.com.

This year, we're launching efforts to link our capabilities in our largest market, Los Angeles, and recently kicked off our efforts with a group of highly engaged customers to co-create unique customer shopping journeys. We intend to apply our learnings from L.A. to quickly scale to other markets.

We continue to see positive trends in customer metrics, which are an important way we measure our progress in gaining new customers and increasing engagement with existing ones. The growth in active customers and customer shopping across multiple channels continues to outpace sales growth, which helps contribute to market share gains.

As we aspire to be the best fashion retailer, our customer strategy is centered on 3 strategic pillars: providing a compelling product offering, delivering exceptional services and experiences and leveraging the strength of our brand.

Now I'd like to turn the call over to Anne to provide additional insights into our financial performance and outlook for the year.

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

Thanks, Blake, and good afternoon, everyone. We had a solid start to the year, reporting Q1 EPS at $0.51.

From a top line perspective, overall sales were consistent with our expectations and reflected strong digital growth. Additionally, credit revenues came in better than expected, the result of our recent efforts to drive new account growth. In full-price, our core U.S. business had stabilized trends. Also, Trunk Club showed significant improvement. In off-price, sales were slightly below our plan, reflecting outsized digital growth, offset by Nordstrom Rack stores' performance. As Blake mentioned, we expect improvements throughout the year.

Turning to gross profit, our rate was down approximately 20 basis points relative to last year. This was due to higher occupancy related to U.S. and Canada Rack openings, in addition to planned preopening expenses associated with the New York Men's Store. Merchandise margins were in line with expectations in the prior year, reflecting continued strength in regular-priced selling trends. We exited the quarter in good inventory position, with sales growth exceeding a 2% decline in inventory.

Our SG&A rate was roughly 30 basis points higher than last year, primarily due to preopening expenses for the New York Men's store. Our SG&A rate performance reflected an improvement relative to recent historical trends as we continue to benefit from productivity gains in marketing, technology and supply chain.

Next, I'd like to provide further insights on our path forward. As we shared in last quarter's call, we expect 2018 to be an inflection point for improved profitability based on the following drivers:

We've made generational investments in Canada and Manhattan and through our acquisitions of HauteLook and Trunk Club. We anticipate operating improvements as these businesses scale.

We're also benefiting from productivity gains as a result of foundational investments in our capabilities. We expect ongoing opportunities for improved expense leverage, particularly in marketing and technology. In supply chain, we continue to invest in creating end-to-end value and improving the customer experience.

Our strategic brand partnerships represent another lever that enables us to provide a compelling product offering and strengthen our regular-price selling.

Now I'd like to take a moment to remind you of our capital allocation principles. First and foremost, our priority is to reinvest in the business to create long-term shareholder value. Over the next 5 years, our CapEx plan of $3.2 billion or 4% of sales supports investments in digital capabilities and new market opportunities in Manhattan and Canada.

In addition, we seek to return capital directly to shareholders through dividends and share repurchases. We recently announced a quarterly dividend of $0.37 per share and resumed share repurchase activity.

And finally, we remain committed to maintaining a strong investment-grade rating.

Turning now to our full year outlook. We've narrowed the EPS range to $3.35 to $3.55, raising the low end to incorporate our first quarter performance. Our first year sales outlook remains unchanged, reflecting a comp sales increase of 0.5% to 1.5%. Our updated EBIT outlook assumes current credit revenue trends at a mid-teens growth rate.

As a reminder, our outlook includes the following sales timing considerations: While comp sales will be reported on a like-for-like basis, total sales will be impacted by shift from the Anniversary Sale.

Additionally, revenue recognition is not expected to materially impact full year sales, but there will be associated impacts related to the anniversary event shift.

These 2 combined factors are estimated to create a timing impact to total sales growth by approximately 150 basis points in Q2 and Q3. Please refer to our appendix for further color.

Finally, before we turn to Q&A, we'd like to announce our plan to host an investor event on July 10. This will give us an opportunity to provide further insights into our customer strategy, how we're positioned for the future and drivers of long-term value creation. We plan to webcast the event and we'll follow-up with more details. Now I'll turn it over to Trina for Q&A.

Trina Schurman - *Nordstrom, Inc. - Director, Investor Relations*

Thank you, Anne. (Operator Instructions)

We will now move to the Q&A session.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question is from Oliver Chen from Cowen and Company.

Oliver Chen - *Cowen and Company, LLC, Research Division - MD & Senior Equity Research Analyst*

Great job on the Men's Store, really innovative with the structure and service and curated assortment. Our question is about digitally enabled sales. What's ahead in terms of improving profitability and margin rates in that over time? And related to that is your comments around supply chain. What would you say are the bigger opportunities just making sure that it's as seamless as possible in terms of the next chapter of the supply chain. You've been really advanced in a lot of the features that you offer, such as geolocation and inventory accuracy. Would love your thoughts.

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

Sure. This is Erik. First one, the digitally enabled sales. First of all, our profitability on those sales is really terrific, it's some of our highest profitable customer engagements that we have. So our goal is not only profitable, more importantly, they're some of our highest satisfaction services we provide. So our focus is to have more customers participate and we have a challenge on awareness. We offer a lot of services in our stores and it's not always as conspicuous to customers what those capabilities are. It's one of the things we've learned at the local store we opened in Los Angeles, by having a store that's all about services, it's been easier to communicate to customers what we can do, and engagement with a lot of those services has been terrific. So we're seeing nice growth in what we call our digitally enabled sales and we'll continue to do that. On supply chain, in general, we're looking to leverage the inventory we have to serve customers better. We think it's an advantage that we have a lot of inventory very, very close to our customers, which is in our stores. Our stores are obviously in the big markets, and that happens to be where the vast majority of our online customers are, too. So a big step in that will be opening a fulfillment center in Southern California. We're just getting underway on plans on that. But we'll be able to -- through that and some other initiatives we're working on, be able to offer our customers much bigger selection at much faster shipping rates. And it also leads to a pretty significant step in inventory efficiency for us, too.

Operator

Our next question comes from the line of Mark Altschwager from Robert W. Baird.

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

Could you provide a bit more color just on some of the comp results in the off-price business? What do you believe drove the softness in the quarter? And did weather play a role at all? And what do you see is the key drivers to the improvement over the remainder of the year that you talked about, and especially on the store side?

Blake W. Nordstrom - *Nordstrom, Inc. - Co-President & Director*

Mark, this is Blake. And I mentioned in the off-price comments that we had a 0.4% increase that was just slightly below our plans for off-price. But within that, we had really strong digital online sales with Nordstromrack.com and HauteLook. But our stores did see some softness in the first quarter. And you mentioned weather. We did see some seasonally related items and classifications impact it, predominantly Women's Apparel. Women's is our largest merchandise division in the Rack. There's a number of initiatives that we're working on. I think the thing that we're most encouraged about is that the customer accounts are flat. So we still have a lot of great foot traffic, and we have a real opportunity if we get the mix and the buy right. Our inventories are in line, so we're fluid. We have open to buy. And we don't believe we have undue risk with markdowns. So we've been able to address that on a daily basis on those things that are underperforming. And so we have -- we fully expect to see improvements throughout this year, both in our plans and our expectations. And we're working hard on a number of initiatives to address those opportunities in Q1.

Operator

Our next question comes from the line of Paul Trussell from Deutsche Bank.

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

I just want to make sure we walk away understanding the spread between comps and sales with the various shifts. So first, I wanted to ask if you could discuss the rewards loyalty event that shifted into 1Q? And while I understand that helped overall sales by 250 basis points, could you just clarify whether or not that is included in the comps? And then, also, looking into 2Q, net sales, you mentioned it would be helped by the inclusion of the Anniversary Sale by 150 basis points. But do we net that out against the 250 basis points shift, I guess, lost from the loyalty event? Help on those items would be greatly appreciated.

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

Sure. Absolutely. 53rd week years are always challenging no matter what company you talk to in the retail space. So let me try and walk you through that. So from a comp perspective, we're looking at this on a like day for like day. So the shift in calendar has no impact to comp sales. The only delta that we laid out is in the appendix slide of the deck that we went through. It's on the Triple Point event, and that's net of several things. It's the calendar shift as well as any impact there was in the quarter for revenue recognition. So we've netted all that together and that part of the spread between comp and total sales growth. When we go to Q2 and Q3 and the rest of that schedule, we netted all of that together for you, so all you have to do is look at it all together between shift in calendar, shifts in events and revenue recognition, and that's just the net impact.

Operator

Next is Dana Telsey from Telsey Advisory Group.

Dana Lauren Telsey - *Telsey Advisory Group LLC - CEO & Chief Risk Officer*

Can you talk a little bit about what you're seeing in terms of the merchandising side of the business, in terms of was it new products that you've had and new brands that are resonating and how it's differing in Rack versus full-line?

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

Dana, this is Pete. It's been part of our initiative for a while to be really explicit and purposeful about trying to bring in new brands. And that's gone really well. The thing that's probably most encouraging is that we see growth and strength across our portfolio. And it's not necessarily because it's new or because it's small or because it's exclusive or because it's a large established brand. It's kind of how it all works together. So in terms of some of the new things we've done that have been successful, we have ALLBIRDS, SWEATY BETTY, Sézane, introduced Anthropologie Home. All that's been really great. But at the same time, we're also having really good designer business in established brands that you know, I mean, Gucci, Valentino and Saint Laurent are all on the top handful of growth brands that we have. Chanel is also in there. So I mean, I think, you see it play out when you look at our men's store for example, it's this kind of unique breadth of offer that we have. And we know that's a recipe that works. It takes a lot of finesse. And we're working on it. And the whole brand vendor part of it evolves all the time, but it's something we spend a lot of time working on and trying to establish collaborative relationships that we're solving for common problems. And I think we're really encouraged by where we are with this and what's possible in the future.

Dana Lauren Telsey - *Telsey Advisory Group LLC - CEO & Chief Risk Officer*

And on the full-line stores, is there any categories of strength, categories that you want to see improve more that we should be looking towards?

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

Well, gosh, I'd say, the one that we want to improve more is probably shoes. We had a challenged Q1 in shoes. A lot of that was related to some of the seasonal stuff that came up earlier if you just look at purely like sandal sales, as an example. Now a lot of that's changed now with the weather has kind of swung all across the country. We're a little bit back on track there. But I'd say, our women's shoe business, if we can get that humming along, that could make a big difference. We've had continued strength in the accessories, handbags, beauty part of our business, which just continues to do really well. You heard me mention the designer part. That's the best growing part of our businesses, is designer across the handbags, the women's apparel and the men's apparel and shoe offerings. And as good as that is, I think, it suggests it could be better. So we think we can do more that way as well. There's a lot to be encouraged about, I think. And again, we talked about the established brands. You've got brands like Lauder or Nike and people like that, that have been around for a long time, and we have good, strong business with them and good collaborative efforts.

Operator

Next is Erinn Murphy with Piper Jaffray.

Erinn Elisabeth Murphy - *Piper Jaffray Companies, Research Division - MD and Senior Research Analyst*

I guess, going back to the digital focus. If you kind of think about furthering that, could you just maybe speak to how that's impacting the number of stores you're thinking about on a long-term basis for both Rack and full-price here in North America? And then, at 29% being digitally enhanced, where do you see this going over time?

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

Erinn, this is Erik. Well, how we look at it, both in full-price and off-price, and I would say we're a little further along in full-price, we have some stronger data, is looking at it by market and really look at within markets, how can we gain market share by leveraging both our digital assets and our physical assets. And so we continue to get better information all the time of the synergy between the physical and the digital. So with that, you've seen us close, I don't know, 2 to 3 stores a year the last couple of years. I think that's probably the best barometer going forward. We certainly don't anticipate large-scale store closings. All of our stores are profitable, both in Rack and our full-line stores. So it's more understanding a market and where we get the best engagement with customers and how that adds up to be profitable relationship with customers. So our focus is market share by local market and how we can grow that.

Erinn Elisabeth Murphy - *Piper Jaffray Companies, Research Division - MD and Senior Research Analyst*

And then, just maybe on active customers. Last quarter, you talked about 33 million active customers. I think it's the first time you've given that metric. Any update to where that was at the end of the first quarter?

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

Yes. So I don't think it's materially changed. And our plan, we try to give some color commentary in the script as far as how we're thinking about the customer. I think that's more of a metric that you'd want to look to on a rolling 12-month basis.

Operator

Next is Matthew Boss with JPMorgan.

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

So a question, at your full-price stores, same-store sales decelerated from a 2.4% comp in the fourth quarter to a 0.7% comp this quarter. Comparison was similar. I know you said sales hit your plan and you spoke the signs of stabilization. But I guess, what do you think accounts for the sequential slowing at full-price, despite what a lot of companies are speaking to as a pretty strong consumer backdrop for your core customer. Just maybe, Blake, any thoughts that you have for that sequential slowing?

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

Yes. So I think a couple of things before we talk about the overall. I just want to get anchored in some of the numbers. So the first thing is when we talk about full-price, that includes stores, our digital channels as well as Canada and Trunk Club in it. So that is all in full-price business. So that's not necessarily a same-store sale. As we mentioned last quarter, it's really gotten very muddy and it's really not -- it's not even how we look at it inside business as well. So it's -- we're really looking at this less on a channel basis and more on a comp and total sales based on full-price and off-price. So that's number one. So when you look at that release that we did, it actually show -- we showed that on a comparable basis. We went it and revised it, so you can see the overall trends in that full-price business. So we actually saw in Q1 against Q1 of last year was actually, it was a positive comp versus last year was a negative comp. So we feel like, in Q1, our full-price business has continued trend, particularly what we saw in the second half of last year.

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

Great. So the 0.7% comp that you did this quarter, what comp did you do in the fourth quarter on an apples-to-apples basis?

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

2.4%.

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

Right. So what accounts for that sequential deceleration from the 2.4% to the 0.7%? That was really the basis of the question.

James F. Nordstrom - *Nordstrom, Inc. - Executive VP & President of Stores*

This is Jamie. I think, one of the things that we saw coming into Q1 was a little bit of a slight deceleration early in the quarter on some of our online traffic, mostly as a result of some changes we made with marketing, it wasn't so much product or execution. Those trends started to shift towards the end of the quarter. So while you're right, it does show a deceleration. I think, there's some puts and takes in Q4. We feel pretty good about how we came out of Q1. Overall, if you look at our business, our full-price business over the last year, really 2 years, it's been incredibly stable and -- in terms of traffic and ticket and average price point, all those metrics. So there's really nothing to point to that would sort of give you any color.

Operator

Next is Chuck Grom with Gordon Haskett.

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

Anne, back in March, you gave us some color on the margin cadence as 2018 progressed. I think you said -- and it's not in slide deck this afternoon, so I just want to ask and see if you could clarify. I think you said the first quarter would be below, second quarter would be above and then the back half would be in line. Operating margins were down about 45 basis points here in 1Q. Just want to see if you still believe in the cadence throughout the rest of the year?

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

So directionally, we do believe that's the right cadence. And clearly, there's going to be a little bit here and there. But when we look at the margins for Q1, it was pretty in line with our expectations. So we would still -- and so the guidance we gave for the ups and downs as well as the full year, we feel, is pretty correct.

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

Okay. And then, just looking ahead on Slide 11, you talked about the planned improvements, it's the second time you've shown that slide. Just curious where you think, when you look out over the next couple of years, operating margins could get to? And I guess, embedded in that, what would be the comp that you will need to get there and what would be the leverage hurdle?

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

I'm sorry, so you're talking about the generational investments?

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

Yes. On Slide 11, when you talked about planned improvement over the next 4 to 5 years.

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

Okay. So as we've been talking about, we've been making investments along the way. And we've had -- we're opening up the stores in Canada with Rack, which we're seeing is really enhancing our penetration and strategy and customer awareness in the Canadian market, and we see that as a big piece of it. And the other big piece that's coming online is the Tower, New York Tower in fall of next year. So as that comes online, that's really going to help margin improvement. And then, we're continuing to see our digital growth, and we talked about this both in the off-price in full-price business. And so we highlighted the fact that Trunk Club's improved and we've also highlighted the fact that we have outsized digital growth in our online business for the off-price.

Operator

Next is Simeon Siegel with Nomura Instinet.

Simeon Avram Siegel - *Nomura Securities Co. Ltd., Research Division - Senior Analyst of U.S. Specialty Retail Equity*

To follow up on an earlier question, just recognizing the puts and takes of the new comp methodology, and I guess, the 53rd week shifts are only impacting drivers. So any help you can give us with expectations for your 2Q comps? Although I think it was a tougher compare. And then, just, Anne, sorry if I missed this, the tax rate, what's the right way to think of that, when does that start to come down?

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

Yes. So we don't normally give guidance as far as comps on a quarterly basis. And so we look at -- we delivered a comp of 0.6% for Q1, and we still have reaffirmed our guidance for the total year. And so, again, we're looking at comps as a true -- or a like day to like day. First is -- and so we gave you guidance and the shift in the calendar for total sales versus comp. The way I would think about the tax rate, it is -- we still are supporting the rate that we gave at the beginning of the year for guidance. But there's just some timing shifts between recognizing profitability within Canada and the U.S. So it's going to be a little choppy throughout the year, but for the full year, it should blend to what we gave you.

Operator

Next is Kimberly Greenberger with Morgan Stanley.

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

I wanted to just follow up on Erinn's question about the optimal store count. Knowing that you're looking at your store count on a market-by-market basis, after you've gone through that analysis and sort of aggregated it up, what numbers are you coming up with in terms of an ideal U.S. store fleet, both for Rack and for full-price? And then, I just wanted to ask, it sounded like the slight miss to plan in the off-price business came from the

Women's Apparel business. Is that -- do you attribute that just to weather? Do you think there were any execution issues? And was that the only business that missed the plan?

James F. Nordstrom - *Nordstrom, Inc. - Executive VP & President of Stores*

Kimberly, this is Jamie. I'll take the first part and hand over to Blake. In terms of store count, we're really not looking at a top-down number. I'd reiterate what Erik mentioned earlier. We're looking at market-by-market. And we have more mature markets. We happen to be calling from Los Angeles right now where we've been doing business for 40 years. Some of these stores, we opened in centers that were once better than they are now and we've got some stores that are in centers that are doing better than ever. And so there's a lot to goes into how we look at it. It's about investing in existing stores. We have a number of stores that we've made big investments in over the last few years and have plans to continue to invest in our best stores. In addition to that, we have a store that might to be the fifth or sixth store in a market that we opened when that made a lot of more sense, I think, 10, 15, 20, 30 years ago. And you've seen us close some of those stores. So it's a combination of investing in our best stores, culling those stores that are in malls that are not as relevant anymore, but overall, looking at it market-by-market and seeing how we can be as effective as possible in serving our customers there.

Blake W. Nordstrom - *Nordstrom, Inc. - Co-President & Director*

So Kimberly, this is Blake. In terms of the Rack or off-price, we have roughly 240 stores. These are very productive stores. And we're very pleased to have a great, robust online business as well. It was just shy of $1 billion last year. So we're in earlier days of trying to understand, as Erik talked about earlier, and Jamie, about looking at it from the customers' point of view and how we can best serve them, both in the physical bricks-and-mortar and also digitally. So we're strategic and opportunistic in terms of new store growth. We don't have a set number. Again, we're about 240. We're opening 6 in Canada this year. We have 6 stores in the U.S. and a relocation. We have 4 slated for 2019. So it's not a set number. It has to meet our criteria. These are all strong stores. So we're not looking to close stores in that. But we do think, in general, that we have a very strong base with that strong digital base to best serve the customer. Your second question was regarding Women's, and you asked about the weather or the seasonal part that I mentioned and were there any other execution issues. Yes, there was. But I think the most material was some bets that we made in some areas that were more seasonally related that, in Q1 at least, didn't play out as well, and the customer voted. Your other question was, were there any other businesses or merchandise areas within the Rack that missed plan. No, I would say, predominantly, the other merchandise areas met or slightly exceeded their plans against. Since Women's is such a large part of the business, it had an impact on it. But across the board, we see lots of opportunities, and that's what we're getting after. We have a number of tests that we're working on right now. This is a business that's pretty nimble and agile. And so we can take those learnings and the feedback we get from our people and the customer, apply it, and literally, within 30 days, get some feedback and make some adjustments. And the fact that our inventories are in line, it's a real strength for us.

Operator

Next is Brian Tunick with RBC Capital Markets.

Brian Jay Tunick - *RBC Capital Markets, LLC, Research Division - MD and Analyst*

Question on the outside growth you're seeing in digital. Is that fulfillment and shipping, et cetera? Is that still having a negative impact on margins? Or have you reached scale? I just haven't heard you guys talk about that being a detriment right now. And then, secondly, of the $3.2 billion in your CapEx plans you're talking about, what is being assumed for DCs and supply chain versus other investments?

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

Brian, this is Erik. I'll take the first one. Our growth in digital -- what's the question?

Unidentified Company Representative

Fulfillment.

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

Fulfillment. Yes, sorry about that. Yes, we -- as you've heard us talk about that, we look at our business as full-price and off-price because the customer journey is very much digital and physical combined. And the impact of digital goes way beyond what's captured in e-commerce sales. Now that being said, when we do break it out as best we can, and it's hard to get precise because there's so much overlap, we break it out, for full-price, our e-commerce profit margins are about exactly the same as our store profit margins. So we don't experience any movement in our operating margins when there's a shift from physical to digital. Anne, do you want to add to that?

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

Yes. So on the CapEx, and if it's helpful, there was a, I think, a slide in the Q4 -- or the last quarter earnings just to highlight between -- so fulfillment was roughly about 20% of our CapEx spend. And if you look at technology and fulfillment combined, it was almost half.

Operator

Next is Paul Lejuez with Citi.

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

Just curious if there was a gross margin impact of the shift on the loyalty event this quarter? And what might be the impact in 2Q? And also, just curious, higher level, how you might characterize the promotional environment out there today relative to recent quarters?

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

So I'll take the gross margin question. We really aren't seeing a shift in the margin component to it. And so, Pete, do you want to take the promotion line?

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

Yes. There's really kind of no news in the promotional environment. It's pretty stable. And in some ways, the things that we've done have mitigated that, given kind of the preferred brands, strategic approach that we're taking with a lot of brands. A lot of that's in response to trying to offset some of the promotional activity. But by and large, if you look at it, it's a pretty, pretty flat system.

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

Okay. And was there any sort of pressure from the slightly below plan sales at Rack? Did you have to promote more heavily there to move through? Anything you could quantify in 1Q on the gross margin line?

Blake W. Nordstrom - *Nordstrom, Inc. - Co-President & Director*

I don't know if there's anything I would call out. There are classifications, whether we've got a glut of inventory that customers are not responding. So kind of isolating case will be like dresses. So we've got a lot of dresses that we're backing up, and so we might take additional markdowns at selected times to move a classification. But it doesn't move the needle for the total gross margin, and it's not apples-and-oranges, what we've done in previous years. So we think we're able to address those slow sellers and maintain our margins.

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

And I would just say that, as I called out in the comments, that our gross margin was pretty consistent with what we were expecting in the year-over-year as well.

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

Okay. And do you expect any pressure in the second quarter as a result of the dresses glut, if that's what we call it?

Blake W. Nordstrom - *Nordstrom, Inc. - Co-President & Director*

No. I think what we're pleased about is we're trying to, in more real-time, address any slow sellers that we have. And we feel very good about how current our inventories are and the risk or exposure to it. And I think that's why Anne and the team felt confident with our full year guidance.

Operator

Next is Michael Binetti with Crédit Suisse.

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

I just want to be crystal clear, and I know you won't help us with the second quarter comp you gave us for the year. But is it your view that to build our comps from here, we start with the momentum in first quarter which, in your mind, is the underlying momentum if we ignore these shifts is the 0.6, and that's not affected by loyalty, and that doesn't come out of 2Q, so we roll that momentum forward and then incorporate some sort of acceleration that Jamie spoke to earlier with some of the digital headwinds early in the quarter rolling off by the end of the quarter? Is that the way that we should be rolling forward here as we think about the near-term underlying momentum of the business?

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

Yes. I think that's pretty fair. I guess, I would say, when we gave the comp guidance of 0.5 to 1.5, it was based on what we were seeing, a pretty consistent trend. We would expect, on the high end of our guidance of the comp, that we're going to see continued improvement in our off-price business as well as continued accelerated growth in digital. You have to contemplate that on the high end. On the low end of our comp guidance, which you would assume is a change in off-price and particularly the Rack stores, really doesn't change that much for the year. So this is kind of the bellwether I would use when you look at the rest of the year.

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

Okay. And then, can we -- just a couple on the margin really quickly here. Is the -- I think you gave some commentary last quarter that first quarter EBIT dollars would be down, and that came through. Second quarter EBIT dollars should be up, third and fourth quarter to be flat. And then, can you help us anchor ourselves on the gross margin impact of the Anniversary Sale moving in, in the second quarter? Can we use the historical analogy to the 2016 shift for how much of the gross margin moves because of the sale?

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

Wow, that's pretty granular. There's a lot going on there. So I think, again, I would encourage you to take a look at comps and build from there on the sum of the calendar shifts then you get to total sales. I think, once you go do that and you look at our historical patterns around things like Anniversary Sale, I think you can kind of massage it with what margin structure would look like and the EBIT pieces to it.

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

I mean, usually, if there's a margin issue related to the Sale, it's after the Sale because we've not sold through well, and then that results in markdowns kind of down the road. So it really doesn't happen in the moment so much.

Operator

Next is Lorraine Hutchinson with Bank of America.

Lorraine Corrine Maikis Hutchinson - *BofA Merrill Lynch, Research Division - MD in Equity Research and Consumer Sector Head in Equity Research*

Just wanted to follow up on the comment that Trunk Club made significant improvements in the quarter. Can you just talk a little bit about why and what your expectations are for that business this year?

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

Sure, it's Erik. Yes, it's -- you're talking about last year, really spent -- the team spent all of last year doing a pretty deep dive and change that took the business model mainly around the Trunk business. We do have clubhouses, but the majority of the business is through the Trunks. So we pulled back on marking last year to get the business model to a point where we think we can scale it. We think we're to that point right now. The last several months, in particular, again, we do it. It's about serving customers better. And our customers' response has been significantly more positive. In particular, it shows up in the keep rates we have from the Trunks we send out and the number of repeat Trunks that customers are signing up for. Both of those metrics are significantly improved from what we've had since we bought the business. So I would describe it as still early days, but we're certainly encouraged that the core of the business, the Trunk business, has a model that is something we're excited about. We're confident that success can continue and it's something we can get behind and start to leverage more.

Operator

Our last question comes from Brian Callen with Bank of America.

Brian Douglas Callen - *BofA Merrill Lynch, Research Division - VP and Research Analyst*

Anne, on an ongoing basis, you continue to run at the high end of your 1.5 to 2.5x long-term leverage range. And I appreciate the comments on IG ratings. I guess, I'm wondering, has the targeted range changed? And then, can you discuss your willingness to sort of flex the balance sheet for additional investment if you find it, share repurchase, M&A or sort of where you'd be comfortable operating from a credit rating perspective, if you find a unique opportunity?

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

Yes. So on the flex side, we are at the top end right now. We do -- we've had, as you know, some of the preopening expenses and some of the investments in Manhattan and Canada. And that's kind of driven that up to the higher end of the leverage range. We still feel very comfortable with that leverage range. As I mentioned in the comments, we're very committed to being a strong investment-grade debt company. And so as we start bringing some of these generational investments more in line with similar growth, we expect to see that leverage to get back into the norm. As far as the flex on the balance sheet, I think, we'll provide -- I think we'll have a lot more opportunity to provide some color in the Analyst Day on that as well. But in general, we do like to -- we have a fairly conservative balance sheet. We do want to be investment-grade. And we do take a look at where is the best return on our investments. So first, investing in the company and driving shareholder value that way and then looking at the best way to return cash to shareholders, whether it's dividends or share buyback. We do take a look at share buyback as a return metric, and we are a little opportunistic as we see the price maybe getting out of balance where we think the intrinsic value is of the company, we'll go be opportunistic in that manner. So -- and from an M&A perspective, again, we've got a very flexible balance sheet. So again, we're looking at what's the best -- right investments and the long-term return for the shareholders.

Trina Schurman - *Nordstrom, Inc. - Director, Investor Relations*

Again, 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. Thank you for your participation.
