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FQ1 2023 Earnings Call Transcripts

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Presentation

Operator

Hello, everyone, and welcome to the First Quarter 2022 DICK'S Sporting Goods, Inc. Earnings Conference Call. My name is Victoria, and I will be coordinating your call today. [Operator Instructions]

I'll now pass you over to your host, Nate Gilch, Senior Director of Investor Relations, to begin. Please go ahead.

Nathaniel A. Gilch
Senior Director of Investor Relations

Good morning, everyone and thank you for joining us to discuss our first quarter 2022 results. On today's call will be Lauren Hobart, our President and Chief Executive Officer; and Navdeep Gupta, our Chief Financial Officer. A playback of today's call will be archived in our Investor Relations website located at investors.dicks.com for approximately 12 months.

As a reminder, we will be making forward-looking statements, which are subject to various risks and uncertainties that could cause our actual results to differ materially from these statements. Any such statements should be considered in conjunction with cautionary statements in our earnings release and risk factor discussions in our filings with the SEC, including our last annual report on Form 10-K and cautionary statements made during this call. We assume no obligation to update any of these forward-looking statements or information.

As required by new accounting rules adopted in the current period, our first quarter GAAP earnings per diluted share assumes share of settlement of our convertible senior notes issued in Q1 2020, which excludes the after-tax interest expense and includes the total shares underlying these notes. Given our intent to settle the principal portion of these notes in cash and the shares that will be delivered by our bond hedged settlements, we do not expect the notes to have a dilutive effect at settlement. Accordingly, we believe that reflecting the notes as debt more closely aligns with the underlying economics of the transaction, which is reflected in our non-GAAP earnings per diluted share. For additional details on this or to find a reconciliation of any non-GAAP financial measure referenced on today's call, please refer to our Investor Relations website.

And finally, for your future scheduling purposes, we are tentatively planning to publish our second quarter 2022 earnings results on August 23, 2022.

With that, I will now turn the call over to Lauren.

Lauren R. Hobart
President, CEO & Director

Thank you, Nate, and good morning, everyone. We are pleased with our first quarter results as our team continued to move with agility and execute well in a highly dynamic environment. Before diving into the results of the quarter, I think it's important to recognize that over the past 2 years, we have demonstrated our ability to adeptly manage through the pandemic and other challenges and we are confident in our continued ability to adapt quickly and execute through uncertain macroeconomic conditions, while keeping our athletes at the heart of every decision we make.

With that context, I do want to take a moment to address the adjustments we made to our 2022 outlook this morning. Like everyone else, we have been carefully monitoring the rapidly evolving macroeconomic environment and assessing our expectations based on our experience running our business across economic cycles. With this perspective, we

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believe it's appropriate to be cautious and are, therefore, lowering our outlook for the year.

To be clear, we expect our performance will continue to meaningfully exceed 2019 levels, reflecting the strength of our core strategies and the changes we've made in our business over the past 5 years. DICK'S is the clear market leader, and we are well positioned to extend our lead and build on our competitive advantages in the years ahead. We continue to closely watch the macro landscape and have the flexibility in our business to remain nimble.

Now getting back to our results. As we announced earlier this morning, we delivered sales of $2.7 billion in the first quarter. This included a comparable store sales decline of 8.4%, which followed a 117% increase in comp sales in the same period of the prior year. This also reflected the anniversary of significant stimulus payments as well as anticipated sales normalization in certain categories.

Importantly, sales continued to run substantially above pre-COVID levels, up 41% versus Q1 2019 and sequentially accelerated from last quarter. These top line results reinforce our strong conviction that the shift in consumer behavior over the past 2 years is indeed structural. Consumers have made lasting lifestyle changes, with an increased focus on health and fitness and greater participation in sports and outdoor activities. Our business is squarely at the center of these secular trends and the actions we have taken over the past 5 years to transform our company have given us significant competitive advantages across all aspects of our business.

Our increasingly differentiated product assortment, combined with our disciplined and more sophisticated promotional strategies, continues to drive strong merchandise margin growth. During the quarter, we expanded our merchandise margin rate by 143 basis points versus 2021.

Before continuing, let me underscore this critical point that is not always appreciated about our transformation. The content of the product that we carry today is very different from the products we carried 5 years ago. It's higher heat and more narrowly distributed than what you'll find in the market as a whole, and therefore, it is not as susceptible to promotion. In addition, the tools we have today to surgically adjust pricing are significantly more sophisticated than they were several years ago. With these fundamental changes, we are very confident that the majority of our merchandise margin rate expansion that we've driven over the past 2 years is sustainable.

Led by our structurally higher sales and merchandise margin compared to pre-COVID levels, we achieved double-digit EBT margin of over 12% and non-GAAP earnings per diluted share of $2.85, both significantly ahead of any pre-COVID first quarter in our history. We entered 2022 in a position of tremendous strength and we're focused on enhancing our existing strategy to further strengthen our core business and drive long-term profitable growth.

Our approach is centered on our best-in-class omnichannel platform, which features our stores as a hub. During the first quarter, our stores enabled over 90% of total sales, serving both our in-store athletes and providing over 800 forward points of distribution for omnichannel fulfillment through ship from store, in-store pickup or curbside. We also continue to invest in an enhanced service model and lean into highly engaging experiences to better serve our athletes and reinforce their loyalty.

Our digital capabilities remain core to our omnichannel success and we are continuing to prioritize investments in technology and data science. Furthermore, we remain focused on maintaining our strong culture, putting our teammates, athletes and communities at the center of everything we do. This work continues to have a positive impact, as we were recently awarded back-to-back annual certification by Great Place to Work. I spend a lot of time visiting our stores and distribution centers and the positive energy and sense of community from the teams I meet is fantastic. Our strong dedicated team and our ability to attract and retain talent are key competitive advantages for us.

Next, within merchandising, our relationships with key brands remain stronger than ever. Our assortment is on trend and we are providing our athletes with enhanced access to the hottest styles across a wide range of categories from the top

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brands in sports. Importantly, we also are ensuring that we have products at prices that address the needs of all athletes. For example, through DSG, our largest vertical brand, we offer high-quality, fashion-forward product at a tremendous value across men's, women's and youth. Our key lifestyle vertical brands, including CALIA and VRST, are also resonating strongly with our athletes and we continue to invest in and grow these brands.

Lastly, our new concepts, including DICK'S House of Sport, Golf Galaxy Performance Center, Public Lands and Going, Going, Gone!, are delivering promising early results. Today, we are really excited to open our third House of Sport store in Minnetonka, Minnesota. House of Sport has exceeded our expectations and has been a great example of the power of elevated service, community engagement and merchandise presentations. We look forward to continuing to refine and grow these concepts, while pulling key learnings into our core DICK'S and Golf Galaxy chains.

In closing, we remain confident in our strategies and our ability to deliver long-term sales and earnings growth. DICK'S has a unique and powerful position in the marketplace. Sports and an active lifestyle are important in all times and now more than ever as we help families get outside together and lead active and healthy lives. Our teammates are united behind our common purpose, which is to create confidence and excitement by personally equipping all athletes to achieve their dreams, especially during these times of uncertainty.

Before concluding, I want to thank all of our teammates for their hard work and unwavering dedication to our business. I'll now turn the call over to Navdeep to review our financial results and outlook in more detail.

Navdeep Gupta
Executive VP & CFO

Thank you, Lauren, and good morning, everyone. Let's begin with a brief review of our first quarter results. Consolidated sales decreased 7.5% to approximately $2.7 billion. Comparable store sales decreased 8.4% following a 117% increase in comp sales in the same period last year. As Lauren indicated, comps were impacted as we anniversaried significant stimulus payments from the prior year quarter. And in addition, we saw the anticipated sales normalization in certain categories that surged throughout the pandemic. And as part of this year-over-year anniversary, transactions declined by 6.4% and average ticket declined by 2%.

Importantly, our sales continue to run significantly above pre-COVID levels. Compared to 2019, consolidated sales increased 41% and sequentially accelerated from the most recent quarter. Gross profit in the first quarter was $984.7 million or 36.7% of net sales and declined 83 basis points versus last year. This decline was driven by 103 basis points increase in supply chain-related costs and a deleverage on fixed occupancy cost of 94 basis points from the sales decrease. These items were partially offset by continued merchandise margin rate expansion. For the quarter, merchandise margin increased 143 basis points as we continue to see the benefits from our increasingly differentiated product assortment, combined with our disciplined and more sophisticated promotional strategies and clearance pricing. We also saw favorable sales mix.

SG&A expenses were $615.3 million or 22.79% of net sales and deleveraged 195 basis points compared to last year, primarily due to the decrease in sales. The increase in SG&A expense dollar is driven by our investment in advertising and hourly wage rates. These items were partially offset by lower incentive compensation expense and $17 million of income associated with changes in the investment values of our deferred compensation plans, which is fully offset by the investment loss recognized in other expense line. In addition, SG&A also included approximately $13 million of COVID-related safety costs in the prior year quarter.

Driven by our structurally higher sales and merchandise margin compared to pre-COVID levels, EBT was $331.9 million or 12.29% of net sales. In total, we delivered non-GAAP earnings per diluted share of $2.85. This compares to a non-GAAP earnings per diluted share of $3.79 last year and $0.62 in 2019.

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Now looking to our balance sheet. We ended Q1 with approximately $2.25 billion of cash and cash equivalent and no borrowings on our $1.6 billion unsecured credit facility. Our quarter-end inventory levels increased 40% compared to Q1 of last year, with product flow improving as the quarter progressed. Looking ahead, we feel good about our overall inventory levels for Q2 and are prepared to continue navigating a dynamic global supply chain environment through the rest of the year.

Turning to our first quarter capital allocations, net capital expenditures were $53.9 million and we paid $46.1 million in quarterly dividends. During the quarter, we exchanged $100 million at approximately 17% of the outstanding principle of our convertible senior notes for cash and unwound the corresponding portion of convertible note hedge and warrants for 1.8 million shares of our common stock. Following this exchange, we have approximately $475 million in aggregate principal amount outstanding. We also repurchased 417,000 shares of our stock for $42 million at an average price of $101.39.

Now let me wrap up with our outlook for 2022. We are pleased with the start of our year and continue to see meaningful growth above 2019 levels. However, as Lauren mentioned, we have been carefully monitoring the economic environment and there are many puts and takes at play. With an increasingly uncertain macroeconomic backdrop, geopolitical environment and a dynamic global supply chain, we believe it is prudent to adopt an appropriately cautious outlook for the year. Thus, we are adjusting our 2022 guidance range.

For the year, we now expect non-GAAP earnings per diluted share in the range of $9.15 to $11.70 and a comparable store sales in the range of negative 8% to negative 2%. EBT is expected to be in the range of $1.05 billion to $1.35 billion, with EBT margins expected to be approximately 10% at the midpoint. This includes additional risk in supply chain-related costs and higher wage rates as well as greater than originally anticipated normalization of promotional landscape over the balance of the year. As a reminder, this also includes approximately $55 million of pretax interest expense associated with our $1.5 billion long-term debt.

Our earnings guidance assumes an effective tax rate between 23% and 24%, and is based on an approximately 88 million average diluted shares outstanding. In addition, our plan now includes a minimum of $300 million of share repurchases, the effect of which is included in our EPS guidance. Importantly, we are continuing to invest in our business for long term, and for the year, expect the net capital expenditure of $340 million to $365 million.

In closing, we are pleased with the results of our first quarter. And while we recognize we are in an uncertain economic environment, DICK'S is a clear market leader, and we remain structurally stronger and more profitable company today compared to pre-COVID. And at the midpoint of our updated outlook, we expect sales to increase approximately 35% versus 2019 and EBT margin of approximately 10%, doubling our 2019 EBT rate. Our financial position is strong, ending Q1 with approximately $2.25 billion of cash and cash equivalents, and we remain confident in our strategy and our ability to drive sales and profitability growth over the long term.

This concludes our prepared comments. Thank you for your interest in DICK'S Sporting Goods. Operator, you may now open the line for questions.

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Question and Answer

Operator

[Operator Instructions] And our first question comes from Simeon Gutman at Morgan Stanley.

Simeon Ari Gutman
Morgan Stanley, Research Division

I would like to follow up on the revision. I think the midpoint, it's about a 16% cut, and Navdeep, you mentioned a few factors. Can you talk to us about the current environment? What's changing as we speak? Sales, gross margin, can you talk about the inventory balance? It looks like you're carrying a good amount going into the year. Are you already seeing that elevated promotion? Are you seeing in line with what's in your guidance? So that's my first question.

Lauren R. Hobart
President, CEO & Director

Thanks, Simeon. It's Lauren. I think those are all very important questions, and I'll try and parse them all out and answer all of them. We have had, as you know, a fantastic, a very good Q1. We're pleased with our Q1. And we had anticipated increases in our freight cost, in our labor costs and in our product costs as we went into the quarter and we were accurate in our forecasting of those expenses.

There's two things that have changed that are driving our approach to the guidance for the rest of the quarter. First is that the consumer is going through an awful lot right now. So obviously, macroeconomic trends are challenging, inflation is putting pressure on the consumer at the gas pump and in grocery store, we all know. And then there's this geopolitical environment that is very, very challenging. At the same time, we see that the expenses of those 3 line items, so freight, labor and perhaps product input costs, are accelerating more quickly than we had anticipated. And so we want to be appropriately cautious as we look forward to the year.

However, I want to be very clear that we are not seeing any meaningful trends that are different from what we saw in Q1 and we believe our inventory at plus 40% actually is very healthy and we are very pleased with it. In fact, there are areas where if we could have more, we would have more. There's been some disruption in terms of when inventory is flowing in. But we had anticipated that certain categories, like fitness and outdoor equipment would normalize this year. And they have normalized as we expected. We are still chasing products in certain categories and our inventory is healthy. We are not anticipating any significant markdown risk.

To answer your other question, our -- the promotional environment, we are not seeing a change in the promotional environment. We will obviously continue to monitor that and we will be surgically addressing price changes as we absorb some of the cost increases. But the marketplace has not shifted dramatically in any meaningful way. We are just being appropriately cautious as we look toward a lot of things that are outside of our control when we look at the rest of the year.

Simeon Ari Gutman
Morgan Stanley, Research Division

Okay. The follow-up is the confidence that the industry or your business won't revert further, and we've been talking about this question for 2 years. But is there any categories that you can point to that -- in which consumption is holding or growing at the structurally higher level? Because we're at a much higher water level, as you mentioned, 30%, 40%,

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even at the midpoint, I think Navdeep said. So which categories are showing us that we won't see that level of reversion?

Lauren R. Hobart
President, CEO & Director

Yes. Across the board, you're absolutely right. If you look at the last 2 years and look at the consumer, every single category in our business has -- virtually everyone except for hunt, has rebaseline meaningfully higher than our pre-pandemic volume. And that reflects the fact that the consumer is outdoors more. They are running, they are walking, they are playing golf. The pandemic-surging categories that we've all been talking about and we expected to normalize are fitness, outdoor equipment, which will include things like bikes and paddles and golf. And those 3 normalize as we expected them to normalize, but we believe they all have long-term growth potential.

So we are not changing our outlook on any aspect of our business. We actually think in these types of times, people need to get outside. They need to be active. They want to be with their families, and we are well positioned to serve the needs of these athletes.

Operator

Our next question comes from Adrienne Yih at Barclays.

Adrienne Eugenia Yih-Tennant
Barclays Bank PLC, Research Division

Great. Lauren, I want to stay on the promo topic because we as well did not see promos this quarter. I guess my question really is the notion that, say, a partnership with Nike, where you're sort of their premier partner, let's just call it, for lack of a better term. Is that causing other competing brands to actually offer you their best and highest heat product as well, so thereby elevating the entire brand and product platform? That's my first question.

Lauren R. Hobart
President, CEO & Director

Yes. So our partnership with Nike is at an all-time high, as is our partnership with all of our strategic partners. And I think that's a result, not just of a situational moment in time with certain partners, but the fact that we have invested so much in our stores and in our experience, such that brands who are rooted in sport want to actually showcase their product and their brand in our stores.

So yes, across the board, we are getting access to higher heat and more pristine premier product that's high in consumer demand. And that's a big part of our strategy, and that has been driving our results.

Adrienne Eugenia Yih-Tennant
Barclays Bank PLC, Research Division

Great. And then for Navdeep, a couple of quick ones. Inventory at the end of the quarter was up 40%. You're comfortable with that. What portion of that is cost inflation, like AUC increase? And what portion of that is in transit? So effectively, I'm trying to get to units, so yes.

Navdeep Gupta
Executive VP & CFO

Yes. Adrienne, maybe before I go into the details, I think one of the ways to think about the inventory is to also look at

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what was happening to our inventory position as we were going through 2021. If you look at it, as we called out last year, our inventory position continued to build as we went into the year. So what you're comparing Q1 versus Q1 last year, especially our inventory starts and in-stock levels last year in...

Operator

[Technical Difficulty]

Hello, everybody, and thank you for standing by. We have reconnected with the speakers. Adrienne, if you would like to go ahead.

Adrienne Eugenia Yih-Tennant
Barclays Bank PLC, Research Division

I think that you were in the middle of your discussion on last year's inventory?

Navdeep Gupta
Executive VP & CFO

Yes. Sorry, I'll start back again. So we apologize. I don't know what happened on the line here. We were -- we seem to be connected here at our end and somehow lost the connection. So Adrienne, back to your question, the way we are looking at inventory. We are looking at inventory trends versus 2019 internally because as we talked about in 2021, our inventory levels were building through the year. So the better comparison for inventory is compared to 2019. So our sales are up 41%. Our inventory is up 32%.

In terms of the balance between in transit as well as unit versus the prices, I would say, yes, we have a little bit elevated levels of in-transit inventory, not necessarily associated with buying the product ahead for the balance of the year. It's much more of -- to do with the product that we expected to receive in Q1 that is slightly delayed. So that's the reason we have a little bit of elevated levels of in-transit inventory. And it's a balance between unit increase versus AUR increases.

Operator

Our next question comes from Kate McShane at Goldman Sachs.

Katharine Amanda McShane
Goldman Sachs Group, Inc., Research Division

I wanted to ask about average ticket, which I think you mentioned was down about 2%. Is there any way to parse out that in terms of how much was price inflation versus how much was the change in mix away from maybe some bigger ticket items during the quarter?

Navdeep Gupta
Executive VP & CFO

Yes. Kate, we haven't given the details on that one. But the way -- the easiest way to think about it is it's a combination. Yes, as you expected and as you called out, that as the COVID surge in categories like fitness and the outdoor equipment normalize, that does put a little bit of a pressure on the ticket size, and that is balanced against the overall AUR increases, inflation related that we have seen.

Katharine Amanda McShane
Goldman Sachs Group, Inc., Research Division

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Okay. And then my follow-up question is, we've heard a lot about adverse weather, whether it be in apparel or auto part retail and just how it affected sales in the first quarter. I know you have some weather-sensitive categories like apparel and team sports in the quarter. Were there any markdowns related to that? And if so, could merch margins have been higher in the quarter?

Lauren R. Hobart
President, CEO & Director

Yes. Kate, we -- it's Lauren. We had -- we did not see a significant weather impact in any of the key categories, certainly didn't drive any markdown behavior. The main category that experienced an impact from the colder and wetter spring was golf. But as I said, that met our expectations of normalizing.

Operator

Our next question comes from Robert Ohmes at Bank of America.

Robert Frederick Ohmes
BofA Securities, Research Division

My follow-up question would be maybe more for Navdeep. I was hoping to get more thoughts on what is implied in the, maybe, the midpoint of guidance. The -- I think, Lauren, you said that the consumer is still doing well into 2Q. Does the midpoint of guidance sort of assume the consumer is going to do less well as we move through the year?

And then also, merchandise margins, really good in the first quarter. Should we expect merchandise margins to look less good kind of sequentially through the year? And then also, you've highlighted these expenses coming through higher than expected. Would you be planning them to accelerate, growth and expenses, to accelerate year-over-year as well?

And also just a clarification on the 2Q to date being similar to 1Q, is that a same-store sales meaning? So should we sort of look for minus 8% to 9% comps in 2Q?

Navdeep Gupta
Executive VP & CFO

So Robert, that was a very in-depth question. Maybe I'll begin with the last question. So one, we're not giving an inter-quarter guidance here. So what we -- the sentiment that Lauren called out is that we are not seeing a material change in the trends of the business. It has much more to do with the customer and not trying to imply anything in terms of the expectations for Q2.

So I'll address 3 big questions that you asked. One is the kind of what is our implied midpoint expectations on the sales. Like Lauren said, Q1, we were pleased with our Q1 performance. The business reaccelerated versus 2019 and especially if you look at where we finished in Q4. So we feel really good about the trends of the business and the core categories in Q1. And like Lauren called out again, like we're not seeing a meaningful change in the trajectory of the business in the month of May.

The takedown in our guidance on the top line expectation is purely coming out of we being appropriately cautious about the outlook on what is happening in kind of the overall economic landscape. The pressure that our consumer and the consumer in general has is something that we wanted to not ignore and wanted to address that upfront. And that has been kind of included in our sales guidance.

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As we think about the other 2 elements that we called out, we have -- we anticipated that the freight expenses would be elevated. There will be inflation as well as there will be wage pressures. But what we are seeing is that these costs have gotten more pronounced in the last 3 months since we gave the original guidance. The fuel prices continue to remain elevated as well as are continuing to go up. So we wanted to acknowledge these risks that we are seeing from a cost structure perspective and we incorporated that in our guidance.

And the last piece, like we called out, right, we anticipated, again, a little bit of normalization of the promotions in the back half of the year. And now we feel that there may be a higher propensity of the promotions in the back half of the year. Again, we are not seeing anything. It's just being cautious about the overall economic landscape and kind of anticipating what might be happening. And potentially, as Lauren called out, we may be seeing -- we are seeing some increase in input costs. And we may decide not to pass all of those costs to our athletes as well, just trying to do the right thing between the athlete as well as the long-term potential of our business. So that is the third piece that has been contemplated into our guidance.

Lauren R. Hobart
President, CEO & Director

Yes. Robby, I just want to build on one thing, which is that our merch margin forecast going forward still assumes, even in the new guidance, that we are going to maintain the majority of our merch margin gains over the past few years.

Operator

Our next question comes from Paul Lejuez at Citi.

Paul Lawrence Lejuez
Citigroup Inc., Research Division

Can you talk about private label penetration and performance during the quarter? And then are there any places where private label is not gaining share within your business?

And then just secondly, if you could just talk about your -- specifically, about apparel and footwear performance and inventory, where you saw strength, where you saw weakness and how you feel about inventories in those categories specifically?

Lauren R. Hobart
President, CEO & Director

Yes. Paul, our vertical brand did extremely well in Q1. And I would point specifically to how pleased we are with the DSG line, and the fact that, that does provide an opening price point with really wonderful fashion is doing incredibly well, as is our new VRST line and our CALIA line. So really, really pleased. And there's not an area I can point to where I think vertical brands are not gaining share across the business.

From an apparel and footwear performance standpoint in the quarter, footwear did really, really well for all the reasons that we've been talking about and inventory in that category is good. And again, if we could chase more, we would chase more. On the apparel side, we did have some inventory challenges during the quarter, just making sure that we have the right product, the right season product in stock. But we are planning to buy around anything that came in late, so it's not a markdown risk for us, and we believe that by back-to-school apparel should be getting better.

Operator

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Our next question comes from Christopher Horvers at JPMorgan.

Christopher Michael Horvers
JPMorgan Chase & Co, Research Division

So I just want to follow up on the merchandise margin point. If I could characterize what you said, you basically, at this point, you have passed through input cost pressures and have essentially at least maintained your gross margin rate. Going forward, you're saying there could be some input cost absorption where it causes degradation in your merchandise margin.

So my follow-up is that if you look on a sort of stack basis versus 2019, merchandise margins did decelerate relative to what you experienced in the fourth quarter. Can you talk about what drove that?

Lauren R. Hobart
President, CEO & Director

I'll start off and pass it over to Navdeep to answer your last question. I want to be -- I want to clarify one thing. We have passed some input cost pressures on to consumers, specifically in hardlines, a little bit in softlines, but we have not been passing through all of our input cost pressures. We have been benefiting from some of our improved assortment, our mix and the fact that we're not promotional. So our merch margins are not reflecting the -- even though they're so strong, it's not reflecting the fact that we've passed 100% of the cost forward.

Now as we look to the future, if costs continue to increase at an accelerated rate, we may have to start passing higher cost increases on. And at that point, we're going to be down at the really specific data-driven pricing optimized level in terms of what the consumer will bear versus what our margin will absorb. And so I just want to clarify that. And then Navdeep, if you can answer the latter part of the question.

Navdeep Gupta
Executive VP & CFO

Yes. Chris, I think there are 2 ways to think about it. Like if you compare it versus -- in fourth quarter of last year, we had called out that we were not promotional. So when you -- and considering how promotional fourth quarter typically is, that benefit was included in our Q4 expectation. We are very pleased with the performance that we have seen from the merchandise margin expansion, especially when you look at it compared to 2019.

Like Lauren called out, we expect to be able to maintain a vast majority of the merchandise margin gains that we have seen over the last 2 years into this year, and that has been contemplated in our guidance as well. We do anticipate that the promotional landscape will not remain as benign as it has been for the last few years. But our expectation is also not that the promotional landscape goes back to where it used to be pre-COVID levels. So it's somewhere -- it's going to be landing somewhere between the 2, and that's the piece that we will continue to watch out.

Christopher Michael Horvers
JPMorgan Chase & Co, Research Division

Okay. So just that -- just so I understand. So then really in the fourth quarter, it was just a lack of normal promotion in the holiday season that caused an extra benefit, where in the first quarter you didn't have sort of that year-to-year effect?

Navdeep Gupta
Executive VP & CFO

Exactly. Q1 is not as promotional of a quarter as you typically expect, right, compared to fourth quarter. And that's kind

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of -- we still were able to expand our merchandise margin, even when compared to Q1 of 2021. And when you look at the merchandise margin expansion versus 2019, we are very pleased with the trajectory that we are holding.

Christopher Michael Horvers
JPMorgan Chase & Co, Research Division

Got it. And then my quick follow-up is the 100 bps of -- was that all freight? Obviously, diesel sort of mid-quarter -- to your points in the prepared remarks, diesel really ripped higher, up 70% year-over-year mid-quarter. So is that all that impact? And sort of how are you thinking about modeling that on a go-forward basis?

Navdeep Gupta
Executive VP & CFO

Yes. I would say there are -- the biggest one is freight, no questions about it. There are 2 pieces, fuel is what we called out as well as like when you think of the fixed expenses and the deleverage that you get when you have a negative 8.5% comp, that is also included. But the vast majority, I would say, was driven by the freight pressures that we saw.

Maybe -- sorry, I'll add to this, that this was not a surprise to us. When you look at that decline, it was more of a year-over-year. We, like Lauren called out, both these expenses, the wage rate pressure as well as the freight pressure that we saw in Q1 was more in line with our internal expectation, what we thought was there will be some normalization, which we are not expecting right now in the back half.

Operator

Our next question comes from Warren Cheng at Evercore ISI.

Warren Cheng
Evercore ISI Institutional Equities, Research Division

I just wanted to ask about your confidence that the majority of the merchandise margin rate expansion is sustainable. So you've talked about some of these tools you've developed to surgically adjust pricing. You've developed some new clearance concepts. Have these tools and concepts been tested in an inventory clearance environment? So as in 1Q, as some of the pandemic winter categories normalize, were there pockets of inventory or situations where you actually had to clear inventories because it hasn't really happened much in the last couple of years? And if so, can you just talk about the -- how some of these tools are changing the realizations that you're getting on these excess inventories?

Lauren R. Hobart
President, CEO & Director

Yes. Thanks, Warren. We have -- we didn't have a substantial amount of clearance with some of those normalized categories that you're referencing because, as I said before, we are going to buy around healthy, good inventory. So it doesn't -- it's not like we started marking things down. That said, our clearance levels are really, really healthy and improved. And that's partly because of our digital marketing tools and the fact that we can be very surgical. We've moved away from any sort of site-wide and store-wide offers to much more specifically targeted either personalized offers or category-led offers.

And then we are having a lot of success with our Going, Going, Gone! concept, where we can get clearance products, both out of the DICK'S store so that we can bring new fresh product in there, but also in Going, Going, Gone! Once we've consolidated the clearance, we can offer it online easier because we don't have safety stock issues at higher prices without having to let it sort of sit for a long, long time. So generally speaking, our tools are really strong.

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Navdeep Gupta
Executive VP & CFO

Yes. Warren, I'll add one more color to what Lauren said. Back to your initial part of the question, which is the confidence that we can hold on to the vast majorities. Again, if you think back to 2019, hunt's penetration has significantly gone down. The vertical brand penetration has significantly gone up and vertical brands, just to remind, 600 to 800 basis points higher margin rate as well as our approach to marketing has significantly changed. So we no longer are doing big promotions that we used to do back in 2019. And those are all structural capabilities that we have developed over the last 3 years that give us tremendous confidence in addition to kind of the price optimization capabilities we have built.

Warren Cheng
Evercore ISI Institutional Equities, Research Division

That's very helpful. And my follow-up is, are you seeing any evidence of trade down, either the private brands are doing really well? Are you seeing those private brands take share from national brands or new customers coming in? Just any thoughts on trade-down behavior that you might have observed in the first quarter.

Lauren R. Hobart
President, CEO & Director

Yes. I don't think that would be an accurate thing to say that we're watching trade down. I actually think in some ways, it's notable that our Gold customer penetration has actually increased, and our sales from that group have been positive, which is evidence, I think, of the fact that people are still spending on categories that are important to them and the fact that our assortment has become so much more premium and attractive and high heat.

At the same time though, at the opening price point, we have -- we've been having success with things like DSG brand, it's accelerated. But I don't think that -- I wouldn't view that as a trade down. I just think it's the right product for this time in people's lives right now. So it's kind of a bifurcated answer.

Operator

Our next question comes from Sam Poser at Williams Trading.

Samuel Marc Poser
Williams Trading, LLC, Research Division

I have 2. One is on the prior guidance you gave, I mean, you sort of gave real direction on the overall gross margin and SG&A. You said that SG&A would likely lever versus '19 by 150 bps. And I think around 640 bps, the gross margin would end up above '19. So could you update those numbers for us?

Navdeep Gupta
Executive VP & CFO

Yes, Sam. I think our -- I think we have given an appropriate level of guidance today and so I won't go into the details. And maybe if there are modeling questions, we can take that off-line. But I would say that there are three big drivers, just to reiterate, as we talk about the updated guidance, especially when it came to profitability.

The first and foremost is the currently updated expectations for the top line range. So that's been contemplated. The freight pressures just -- and supply chain pressures, which kind of sit between -- which sits primarily in our gross profit line. And then the wage pressure, which if you think about it, is predominantly in our store labor line and that will be on an SG&A line. So that's being contemplated. Potentially, there are other inflationary pressures as well, but we have

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taken some actions as part of the revised guidance that are kind of offsetting the pressures that we are seeing in other lines.

Samuel Marc Poser
Williams Trading, LLC, Research Division

And then during the crisis, you guys did a good job of sort of adjusting to better face your consumers and we're able to internally overcome a lot of the macro craziness that's going on. This is a little bit different coming the other way. What are -- I understand you're sort of being prudent about what could happen. But I guess the question I have is what are the -- what are you doing to sort of raise your own game to overcome these macro pressures that you would -- that caused you to adjust your guidance?

Lauren R. Hobart
President, CEO & Director

Yes. Sam, I will agree with you that I think our team did an incredible job managing through crisis, and we found a few things about our business. One is that we have somewhat of a -- maybe an overstatement, but a natural hedge within our business, such that when people stop playing team sports in that case, they still wanted to get outside with their families. And so we saw other businesses increase. And then similarly, when people started to go back onto the field, you see those businesses normalize. So generally speaking, I think we're in a great lane in terms of the products that we carry.

We are being prudent. Looking forward, we just -- the consumer is going through an awful lot right now. And frankly, it's getting more challenging every single day. And so we will work like heck to pull every lever that we have to drive sales and to manage expenses, and you can expect us to do that. But we want to be appropriately cautious, given how rapidly some costs are accelerating and that the consumer is really in a very challenged state right now.

Operator

Our next question comes from Michael Baker at D.A. Davidson.

Michael Allen Baker
D.A. Davidson & Co., Research Division

Two questions. One, just on the comp, it's fair to say that the new guidance range down -- I think it was down 2% to down 8%. That does anticipate some change in the consumer environment because you're not seeing it yet. But again, I guess you're saying in your guidance, you are assuming some of it, but the second part of that question is, I presume that you still -- you are still running within your previous guidance of 5% to down 4%, because you're not seeing any change, you're just taking it down based on what you think might -- or being cautious on what could happen. Is that the right interpretation of the change in the top line?

Lauren R. Hobart
President, CEO & Director

Michael, I think you said it perfectly. That is exactly that our new guidance anticipates, that there's a lot of things that we can't control going forward. But we are still operating and expect -- within our guidance range on the comp side is absolutely our old guidance, and we are expecting to -- everything we can control, we feel really, really positive about.

Michael Allen Baker
D.A. Davidson & Co., Research Division

Okay. Yes. That makes sense. One other question, if I could ask specifically about the golf business. I think you said

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quickly in there at one point that, that business wasn't as strong. And maybe that was weather related, but you had anticipated that. I guess what's your outlook for the golf business for the year? If there was a weather impact, now that the weather seems to have gotten a little bit better, do we expect that business to get better? Just curious how you're thinking about that category.

Lauren R. Hobart
President, CEO & Director

Yes. Golf is a category that we think has tremendous growth in the long term. Rounds played are still really, really strong. The new consumers who have come into the game have not dropped it and are buying new products. So I think there's going to be some normalization, which we expected. The weather shifts don't bother me at all because that happens every year, one either snowing in December or maybe snowing in April, I don't know. But long term, we have a lot of confidence in the golf business.

Michael Allen Baker
D.A. Davidson & Co., Research Division

Makes sense. And I'll just say your Golf Galaxy offering, the club fitting, I took advantage of that, tremendous offer. Appreciate it.

Lauren R. Hobart
President, CEO & Director

Michael, wonderful. Thank you. We appreciate that. Thank you.

Operator

Our next question comes from John Kernan at Cowen.

John David Kernan
Cowen and Company, LLC, Research Division

So from what we're hearing from a lot of the softline vendors, apparel footwear vendors, the athletic brands, there's plans for an acceleration and in some cases, a meaningful acceleration in their North American businesses as we get into the back half of the year. Can you talk to that opportunity and what you're seeing in that market? How you're buying to that trend as we get into the back half?

Lauren R. Hobart
President, CEO & Director

John, we do see and we guided originally to the fact that we think the year is going to start off -- sequentially accelerate as the year goes on. I mentioned in my remarks that softlines, in particular on the apparel side, have had some supply chain challenges and that we're bullish as we look at more back-to-school in the rest of the year. So I think the consumer is there and the product is good, and we are absolutely buying into these trends.

John David Kernan
Cowen and Company, LLC, Research Division

Got it. And then maybe just on the -- if we look at the high end and the low end of guidance, the down 8% to down 2% and then the $9.15 to $11.70 on EPS, what do you think is the biggest swing factor in the guidance, both from a sales and margin standpoint? What gets you to the high end? And what's the scenario where we're more towards the low end from a macro standpoint? Go ahead.

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Navdeep Gupta
Executive VP & CFO

John, I would say the biggest overriding factor is comp sales. The -- if we continue to see that the consumer is holding up well, and we are not -- and it's not getting impacted by this cumulative impact of inflation, gas prices, commodity prices increasing, if the consumer continues to hold well, that, to me, would be a good indication of how our business will do. And so to me, that is the biggest factor that we are looking into. The cost, yes, we know those will continue to remain elevated. Those have already been incorporated. And so the biggest factor is going to be the top line expectations.

John David Kernan
Cowen and Company, LLC, Research Division

Got it. And then maybe just one quick follow-up there. When you look at -- simplistically look at inventory growth on the balance sheet on a dollar basis versus where we are from a top line growth perspective, pretty much across the industry, what gives you such confidence that we're not going to be over-inventoried into the back half of the year right now? And this goes to the vendors and the retailers, inventory is clearly trending above sales trends at this point.

Lauren R. Hobart
President, CEO & Director

Go ahead, Navdeep.

Navdeep Gupta
Executive VP & CFO

Yes. I think to me, this is where -- on the confidence that our merchandising team come from and the supply chain team. They have a very good pulse on the business, and we have perfected this art on -- as we called out at the beginning of the last 2 years on the upside, and we are very, very careful about thinking about different scenarios, what are the potential, where are the categories where the business could be impacted. And as you expect, that we are doing all of these internal evaluations a lot, discussing about different scenarios. And to me, the confidence that we have in our team is probably the biggest indicator of the overall confidence that we have on our inventory position. Yes.

Lauren R. Hobart
President, CEO & Director

And I think the fact that wherever we are -- where we are right now, the inventory is not toxic. We don't plan to create any level of risk with toxicity, and we can manage through and buy around any inventory we have. So this does not concern us.

Operator

Our next question comes from Joe Feldman at Telsey Advisory Group LLC.

Joseph Isaac Feldman
Telsey Advisory Group LLC

I want to go back to -- on the gross margin line, I know we've talked about merch margin a lot, but you actually mentioned that occupancy costs deleveraged quite a bit. And I just was curious as to what drove that. Was it simply just the sales? Or are you actually seeing rents going up? Or was there incremental pressure related to the real estate side of things?

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Navdeep Gupta
Executive VP & CFO

No, Joe, it's all driven by sales. So -- and at a minus 8.5% comp and 7.5% sales decline, it's all being driven by sales decline. To answer your question, the flexibility that we have in our real estate portfolio and the strength that we have in terms of our financial performance and the strong balance sheet, we actually feel really good about the opportunity that we have to be able to drive more efficiencies in our occupancy costs.

Joseph Isaac Feldman
Telsey Advisory Group LLC

Got it. That's great to hear. And then kind of a bigger picture question I had was, as you think -- or as we all start to think about what's the right level of operating profit going forward or operating margin, EBIT margin, if you will, I mean, how should we think about that? I think we all agree it's probably not going back to pre-COVID levels. It's also probably not going to be at the peak of last year, 16.5%. But 3 months ago, we all thought it was going to be more like 13-ish, and now we're thinking it's 10-ish. So I'm just kind of curious if you can give us any kind of help around that to think about the future?

Operator

Thank you, everybody. Unfortunately, we lost connection with the speakers. [Operator Instructions]

[Technical Difficulty]

Hello, everybody. We have the connection with the speakers again. Please continue the Q&A.

Navdeep Gupta
Executive VP & CFO

Joe, this is Navdeep. I don't know where we got dropped off. I'll try to probably rephrase the last part of my sentence. Basically, what we are saying is that structurally, there's nothing that we believe is going to hold us back from achieving kind of the profitability levels that we saw in 2021. What -- the thing that is at play is the macroeconomic conditions. So to me, that's the piece that we will continue to look to. And structurally, our merchandising margin is really strong, our e-commerce business continues to be really strong, and it's very profitable. So structurally, when you think about it, we are very optimistic about the long-term sales and the profitability of our business.

Operator

This concludes our Q&A session. I would now like to pass back over to Lauren Hobart, President and CEO, for any final remarks.

Lauren R. Hobart
President, CEO & Director

Thank you, and thank you all for your interest in DICK'S Sporting Goods. We apologize for some of the technical glitches on this call, but hopefully, you were able to hear the confidence that we have in our business. We look forward to seeing you next quarter. Thank you.

Operator

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