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# EDITED TRANSCRIPT

PIR - Q4 2014 Pier 1 Imports, Inc. Earnings Conference Call

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## OVERVIEW:

Co. announced FY14 EPS of \$1.01. 4Q14 total sales were \$516m, resulting in net income of \$43m, and EPS of \$0.41. Guidance was given for FY15 EPS of \$1.16-1.24.



APRIL 10, 2014 / 3:00PM, PIR - Q4 2014 Pier 1 Imports, Inc. Earnings Conference Call

## CORPORATE PARTICIPANTS

**Bryan Hanley** *Pier 1 Imports, Inc. - Director of IR*

**Alex Smith** *Pier 1 Imports, Inc. - President & CEO*

**Cary Turner** *Pier 1 Imports, Inc. - Senior EVP & CFO*

## CONFERENCE CALL PARTICIPANTS

**Budd Bugatch** *Raymond James & Associates - Analyst*

**David Berman** *Berman Capital - Analyst*

**Alan Rifkin** *Barclays Capital - Analyst*

**Anthony Chukumba** *BB&T Capital Markets - Analyst*

**Adam Sindler** *Deutsche Bank - Analyst*

**David Magee** *SunTrust Robinson - Analyst*

**Brian Nagel** *Oppenheimer & Co. - Analyst*

**Brad Thomas** *KeyBanc Capital Markets - Analyst*

## PRESENTATION

### Operator

Good morning, ladies and gentlemen, and welcome to the Pier 1 Imports fiscal 2014 fourth-quarter and year-end earnings call. At the request of Pier 1 Imports, today's conference call is being recorded. (Operator Instructions). I would now like to introduce Bryan Hanley, Director of Investor Relations for Pier 1 Imports. Please go ahead.

### Bryan Hanley - Pier 1 Imports, Inc. - Director of IR

Thank you and good morning, everyone. Prior to market open today we issued a press release which included the detailed financial results for the fourth quarter and full fiscal year ended March 1, 2014. In just a few moments we will hear comments from Alex and Cary about the financial results, the financing transactions announced today and the Company's outlook and fiscal 2015 guidance followed by a question-and-answer period.

Before we begin I need to remind you that certain comments made during this call may contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, and can be identified by the use of words such as may, will, anticipates, believes, expects, estimates, intends, plans, projects and other similar words and phrases.

Our actual results and future financial condition may differ materially from those expressed in any such forward-looking statements as a result of many factors that may be outside of our control. Please refer to our SEC filings, including our annual report on Form 10-K, for a complete discussion of the major risks and uncertainties that may affect our business.

The forward-looking statements made today are as of the date of this call and we do not undertake any obligation to update our forward-looking statements.

The Company will also discuss non-GAAP financial measures on this conference call. Pursuant to the requirements of Regulation G and Item 10E of Regulation SK, the Company has provided reconciliations of the non-GAAP financial measures to the most recent directly comparable GAAP financial measures in our earnings press release that was issued earlier this morning.



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If you do not have a copy of today's press release you may obtain one, along with copies of the prior press releases and all SEC filings, by linking through to the Investor Relations page of our website, pier1.com. Now I would like to turn the call over to Alex Smith, Pier 1 Imports' President and Chief Executive Officer. Alex?

### **Alex Smith** - Pier 1 Imports, Inc. - President & CEO

Thank you, Bryan, good morning, everyone, and thank you for being on today's call. As always I am joined by Cary Turner, our Senior Executive Vice President and Chief Financial Officer. Also around the table with us are other members of my leadership team.

Fiscal 2014 was a transformational year for Pier 1 Imports. Even though we encountered some challenges along the way and concluded with a tough fourth-quarter, we made excellent progress in the execution of our 1 Pier 1 strategy as we rapidly evolved from our store only business model to full omni-channel capabilities.

As we previously noted, sales and earnings in the holiday quarter were pressured by the significant weather disruption, two-thirds of our Q4 trading days. This was extremely frustrating given the superior execution on the part of our teams at all levels of the organization.

I have always said that at Pier 1 Imports we know how to do holiday well. And I can tell you with absolute certainty that we were prepared to deliver another great holiday season. If not an A+++ , our holiday execution was certainly a strong A. The quarter was disappointing for all of us at Pier 1 Imports and for our investors as well. However as bumps in the road go, this was navigable and is now behind us.

So we move forward with great confidence and our heads held high. Our ability to operate stores profitably is proven. And as we execute our 1 Pier 1 strategy and bring the Pier 1 Imports experience to more and more customers we will grow our skills and business with confidence. I know that we will be successful because we are ambitious, we are talented and we have built an optimistic and success focused culture which will guide our way.

Through our 1 Pier 1 strategy we can maximize our selling opportunities, extend our brand reach and capture greater market share. In fiscal 2014 our e-commerce business reached 4% of total sales for the year. It is growing rapidly and yes, there is so much untapped potential for us.

Traffic to our website continues to grow and presently stands at close to 2 million visitors a week, that is nearly double what it was just one year ago. But our conversion rates, although much improved, are still very modest so our upside is huge. Our prospects for growth with our market share are practically unlimited and this is the single most important theme in our prepared remarks today.

One of the critical components of 1 Pier 1 is our new POS system which was fully implemented this past August. Our stores are now positioned to more effectively serve as a gateway to our e-commerce site. As you know, a central part of our strategy is to operate our stores and e-commerce site as mutually supportive and interdependent businesses.

We are becoming less and less concerned about where a sale originates. We let our customers choose. Our single focus is to ensure that our customer has an extraordinary experience regardless of how she shops with us. Our field and store teams have truly embraced this concept.

We are delighted at the percentage of our e-commerce sales that are being placed from the cash wrap PCs in our stores facilitated by our terrific associates. We plan to make ordering from 1 Pier 1 -- from Pier1.com even easier in the stores. We have been piloting the use of tablets in-store and plan a rollout during fiscal 2015. Our ability to leverage our stores in this way is a significant competitive advantage.

Through Pier 1.com we added many more customers in fiscal 2014 and are learning a lot about their shopping preferences. And we are discovering that our omni-channel customers, while still small in number, are extremely valuable.

Customers who shop Pier 1 Imports both in-store and online spend nearly four times our average in-store only customers. When we can convert our customers to in-store and online and engage them through our Rewards card they spend even more.



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To that end we acquired a record number of new Rewards credit cardholders in fiscal 2014 bringing the total number of cardholders to 2.5 million. We exceeded our short-term penetration target of 30% which came in at 34.4% for fiscal year 2014. This is a considerable milestone for us, but we see no reason that participation will not continue to improve. In fact, we are raising the bar higher and now are targeting 35% of sales penetration under the program.

As a side note we are also seeing that as a group our online only customers are slightly more affluent than our store only customers, which opens up some intriguing avenues for assortment expansion.

As we have previously talked about, in fiscal 2014 we rebranded and relaunched our Express Request program in-store which increases the available options for the store shopper very significantly. Customers can choose from an extended range of styles, sizes and colors and pick up their purchases in store within 10 days.

Our customers really love this program; it is growing at a tremendous rate and accounted for more than 13% of our total sales last year, up almost \$100 million versus fiscal 2013.

Now in the first few weeks of fiscal 2015 Express Request is continuing to remain an exemplary pace, up some 60% over the same period last year. And it will continue to expand. Express Request together with Pier 1.com afford us the opportunity to significantly broaden our assortments going forward for our in-store and online customers alike. For our online customers Express Request SKUs are simply part of the available assortment.

Through 1 Pier 1 we have already been able to provide our customers with many more products to choose from by introducing new categories and offering expanded assortments. We also continue to strengthen our logistics and supply chain and now have the capability to offer our customers multiple delivery options.

Most recently we have rolled out in-home delivery to the lower 48 states. Our in-home delivery service offers choice of room or complete white glove service and makes 100% of our SKUs available online including our very powerful Express Request assortments. The average ticket on in-home delivery is in excess of \$1,000.

Turning to our Pier 1 Imports stores, in fiscal 2014 we continue to focus on the quality, not the quantity, of our real estate, strengthening the Pier 1 Imports portfolio during the year through new store openings, which were primarily strategic relocation upgrades to many of our existing locations. In the last three years we have remodeled or refurbished more than half of our portfolio.

Our national footprint has made a major strategic advantage for Pier 1 Imports and our 1 Pier 1 strategy. Our stores, extremely profitable in their own rights, are a gateway to Pier1.com and ambassadors for our brand and, as I have said, have picked up this role enthusiastically.

We will continue to finesse our real estate strategy as Pier1.com gathers strength. Our 1 Pier 1 strategy is about the customer and ensuring the business has flexibility to engage with our customer on a personal level in the way they choose. It is about making shopping easier and more enjoyable.

As I have described, fiscal 2014 was clearly a year of progress, accomplishments and learning on many fronts. From a financial perspective in fiscal 2014 our comparable store sales grew 2.4%, gross profit dollars were essentially even with last year at \$746 million and earnings per share came in at \$1.01 and cash generated from operations was \$159 million. These results are not what we expected at the outset of the year and we are frustrated that we missed the mark.

That said, I am highly confident that Pier 1 Imports is positioned for substantial growth in the coming years. We are truly at a pivotal point in our 52-year history. We are confident in our vision, we have the resources and infrastructure in place to scale the business and we are at the beginning of a new chapter as we tap into the enormous potential that our omni-channel strategy gives us.

As you know, we have generated strong cash flow in recent years. This has enabled us not only to make considerable investments back into the business to drive growth, but also consistently return value to our shareholders through share repurchases and cash dividends.



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Including the repurchases made in fiscal 2014 and here in the first part of fiscal 2015 we have now returned over \$0.5 billion to our shareholders in the last three years through share repurchases and cash dividends. That equates to about one quarter of our average market capitalization and we are happy to see our share count comfortably below 100 million.

In addition, we just announced our next quarterly cash dividend which we recently raised. This is the third consecutive year of dividends since we reinstated our quarterly dividends. And today we announced that our Board of Directors has authorized a new \$200 million share repurchase program as a continuation of our long-term capital allocation strategy.

We have demonstrated our commitment to delivering value which is something you can expect to see going forward. We also have a strong track record of growth that we believe we can resume this year. Our first priority of course continues and must be to invest in the business to drive growth. And for fiscal 2015 we are forecasting comparable Company sales growth which includes e-commerce in the high-single-digits and earnings per share growth of 15% to 23%.

We are well on track with our goal to have 10% of our business coming from e-commerce by the end of fiscal 2016 as set out in our three-year growth plan. Under the plan we had previously expected to reach \$225 of sales per retail square foot and operating margins of 12% by the end of this year which is our fiscal 2015. We have pushed those targets back by one year and established new goal of \$225 in sales productivity and 11% to 11.5% in operating margin by the end of fiscal 2016.

Although we have not yet fully realized the efficiencies of scale and experience, we can already see that our online business will at the very least be as profitable as our stores.

Executing our 1 Pier 1 strategy has required investments over the last three years in systems, fulfillment centers, call centers and distribution networks. We have added to our merchant team to meet the demands of our fast-growing SKU counts. We have added to our marketing team and expanded our photography studio and of course the team that manages and drives our online business.

We will continue to invest in FY 2015 but prudently and only when we are clear that the returns are good or that the workload justifies it. All this is required to support the business that will more than double in size.

Investment is putting pressure on our near-term operating margin percent target. But our goal is to deliver profitable growth but at the same time we must balance profit in the near term with making the investments necessary to sustain growth into the future.

Sales growth in fiscal 2015 will be substantial. Looking at the key sales growth drivers for this year -- first, we are expanding our assortments. Specifically we are planning to quadruple the number of SKUs available online. Our e-commerce site provides a highly efficient method for increasing our assortments and testing new products in categories such as bedding.

This year our customers will see expanded sizes and colors in rugs, wall art, mirrors, wall decor among others. She will also see additional sizes, functions and colors across all furniture categories including an expanded assortment of outdoor furniture and textiles.

By the end of fiscal 2015 we expect our total SKU count to be in the region of 11,000, a 30% increase over the 8,500 that we ended fiscal 2014 with. We know that increased breadth of assortment is a big driver of online sales.

Fortunately, because we run our business with a single inventory and our planning and allocation capabilities are so sophisticated, we expect our inventory growth to be well-controlled as it was in fiscal 2014. Our merchandise and field teams are well prepared for this level of expansion.

To support our growth we will continue to build greater flexibility and capacity into our distribution network. I have already mentioned in-home delivery. The big news for fiscal 2015 is that with the growth we are experiencing online we have brought forward the building of our second fulfillment center by a year. Our new facility in close proximity to our Columbus, Ohio DC will be operational in the fall of this year, freeing up capacity and giving us redundancy.



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We are also actively developing a strategy to utilize all of our DCs as fulfillment centers for large items, further leveraging our single inventory.

Traffic to Pier1.com continues to grow at a rapid pace. As I mentioned earlier, today we are averaging close to 2 million visitors per week and with the Easter build and some decent weather our Pier 1 Imports stores are also enjoying good traffic.

Our customers love coming into our stores to get inspired and receive expert advice from our associates. She can go online and get inspiration from our photographs, editorial pieces and expanded product offerings. Our 1 Pier 1 strategy puts our merchandise at her fingertips whenever she wants to shop with us whether it is in-store, at home or on the go.

Our Easter product has sold through much quicker than last year and initial response to our expanded outdoor assortment is just where we hoped it would be.

It is of the utmost importance that as our business grows and evolves under 1 Pier 1 our marketing strategies stays one step ahead, just as we have done with other aspects of the business. We continually invest in marketing and also in the people who bring our brands to life.

I was extremely pleased to be able to welcome Eric Hunter to my leadership team last year. He brings with him considerable experience in brand strategy, digital and multi-brand marketing. Working with a talented marketing team, Eric's experience will allow us to make great strides in support of 1 Pier 1.

Our marketing plan combines both retention strategies for current customers and acquisition strategies to ensure that we always have new customers joining the brand. We carefully balance our marketing investments across vehicles to best engage with our customers.

We recently launched a new television campaign, a continuation of our Find What Speaks to You campaign from the last few years but with a fresh twist that will inspire customers to shop with us. In order to continue to drive conversion and gain market share in the e-commerce space we are implementing a stronger digital marketing plan for fiscal 2015.

The digital marketing plan, the digital marketing team focuses on email, social, mobile display, search engine optimization and much more. It sounds like a lot and it is. And as we progress under our 1 Pier 1 strategy the size and relevance to our overall plan will keep step. And remember, digital marketing not only drives traffic to Pier1.com, but importantly to our stores as well. As we move forward we will continue to invest 5% of sales into marketing.

We are extremely proud of our website, but also realistic. We know we have much to add in terms of functionality. We also know that the curation of our unique and special products needs to get better. We need to do full justice to our amazing assortments.

We also need to make sure that our site is as attractive on tablets as it is on PCs. These are all priorities for fiscal 2015. The development of our online business is thrilling and exceeding our original expectations.

An exciting addition coming to our stores this year is a newly developed swatch station where customers can browse ideas for fabric color and design. We believe this will help leverage Express Request and Pier1.com driving incremental sales to our already strong rug, furniture and textile businesses and lending a footing to new and expanded assortments. Customers will also be able to order swatches online starting in the early fall.

Turning now to our stores. Fiscal 2015 will mark the third and final year under our capital allocation program designed to upgrade the quality of our real estate. We have made tremendous progress during the first two years driving greater productivity out of our stores and generating strong returns on our investments. In fiscal 2015 we plan to open approximately 30 new stores and close 25, most of which will be relocations.

We are embarking on what we expect will be a successful year. We are a fundamentally different company from where we were when I joined Pier 1 Imports in 2007. We have nurtured a strong and talented organization at all levels.



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We have returned value to our shareholders through share repurchase and cash dividends and we demonstrate our ability to deliver strong growth in sales, earnings and operating cash flow. Strategically I believe we are in the best shape we have ever been and look forward to a year of strong growth in fiscal 2015.

Our Board of Directors shares our conviction, which is evidenced by the additional 200 million share repurchase authorization which we announced today. We have wonderful talented and dedicated associates at Pier 1 imports and I want to thank them all for what they do for our well loved Company every day. Now here is Cary.

### **Cary Turner** - Pier 1 Imports, Inc. - Senior EVP & CFO

Thank you, Alex, and good morning, everyone. First, touching on the fourth quarter, total sales for the 13-week period were \$516 million representing a decline of 6.5% versus the 14-week period from last year. As a reminder, we estimate the 53rd week in fiscal 2013 contributed approximately \$29 million to total sales and \$0.03 to earnings per share.

Fourth-quarter comparable store sales declined 4.6% on the 13-week basis. After adjusting for the calendar shift comparable store sales for the 13 weeks ended March 1, 2014 increased 60 basis points versus the 13 weeks ended March 2, 2013.

Fourth-quarter gross profit decreased to \$214 million compared to \$255 million last year. As a percentage of sales, gross profit came in at 41.6% versus 46.2% a year ago. Approximately one-third of this decline was attributable to a deleveraging of occupancy which was \$73.2 million or 14.2% of sales compared to \$70.5 million or 12.8% of sales last year.

The remaining two-thirds of the decline is primarily due to a higher mix of e-commerce sales for the quarter coupled with an increased level of promotional activity and the clearing of seasonal inventory which is more than anticipated due to the weather disruptions. However, this allowed us to enter fiscal 2015 in a clean inventory position.

Turning to expenses, we maintained strict control over costs during the fourth quarter especially variable expenses which as a percentage of sales were relatively flat year-over-year. In addition, relatively fixed expenses improved approximately 40 basis points as a percentage of sales compared to last year primarily due to the Company not achieving its profit goals under its short-term incentive program.

Fourth-quarter SG&A expense totaled \$134 million compared to \$145 million a year ago and as a percentage of sales, SG&A leveraged slightly to 26.0%. Net income for the 13-week period was \$43 million or \$0.41 per share. During the fourth quarter we opened three stores and closed five for a total of 27 store openings and 17 closings in fiscal 2014. We ended the year with 1,072 Pier 1 Imports stores including 991 locations in the US and 81 in Canada for a total of 8.5 million retail square feet.

For the full-year total sales increased 5.7% compared to the 52 weeks ended February 23, 2013. Comparable store sales increased 2.4% on a 52-week basis. Sales productivity for the year came in at \$202 per retail square foot. That is up from \$198 at the end of fiscal 2013. This year we expect to make great strides against our near-term goal and to reach \$225 per square foot that we now anticipate will hit in fiscal 2016.

Sales on the Pier 1 Rewards card at the end of the year remained robust and accounted for 30.4% of US sales up from 25.7% at the end of last year. As Alex mentioned, this exceeded our initial Rewards card penetration goal of 30%. As we continue to expand our cardholder base and more effectively engage those customers through the use of personalized marketing we believe sales penetration can reach 35% of sales.

Returning to the income statement, full-year gross profit was essentially flat at \$746 million compared to \$743 million for the 53 weeks last year. As a percentage of sales, gross profit declined by 150 basis points to 42.1%. For fiscal 2015 we expect gross profit as a percentage of sales to be approximately flat or slightly better than fiscal 2014.

We believe the growth in sales will enable us to leverage occupancy and offset the drag on the merchandise margin rate that will result from both a continued promotional stance for the foreseeable future and an increased percentage of the business being derived from our direct to customer sales through Pier1.com.



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SG&A expenses for the year were \$531 million compared to \$513 million last year. As a percentage of sales, SG&A leveraged slightly by 10 basis points. Again this leverage was primarily attributable to the Company not meeting its profit goals under the short-term incentive program I touched upon earlier. Full-year marketing spend is on plan at approximately 5.1% of sales.

The Company generated full-year EBITDA in excess of \$200 million. In fiscal 2014 EBITDA came in at \$215 million which compares to \$232 million in the prior year. Depreciation and amortization was \$39 million for the full-year and is expected to be about \$47 million in fiscal 2015. Operating income for the year was \$176 million or 9.9% of sales compared to \$199 million or 11.7% of sales last year.

Turning to the balance sheet, inventory at the end of the fourth-quarter totaled \$378 million, up 6.1% versus last year. That level is in line with the expectations we laid out at the end of the third quarter. We are planning for growth in inventories to be generally in line with the growth in sales at the end of fiscal 2015.

The Company remains in strong financial condition and ended the year with \$127 million of cash and cash equivalents and no cash borrowings under our \$350 million credit facility. In fiscal 2014 generated strong cash flow from operations of \$159 million. The Company paid approximately \$22 million in cash dividends during the year and utilized approximately \$200 million to repurchase 9.3% of its common stock.

Subsequent to year-end we have utilized an additional \$90 million to repurchase another 4.5% of shares outstanding. As Alex pointed out, we have now returned a little over \$0.5 billion to shareholders in the last three years through cash dividends and share repurchases.

With respect to share repurchases the weighted average cost across all of these programs has been \$16.55. As demonstrated through the execution of our repurchases we have taken care to be opportunistic with respect to our share price valuation.

As we announced in today's press release, we made the strategic decision to seek a \$200 million senior secured term loan B facility. We believe this will further enhance our capital structure and provide us with greater flexibility as we continue to utilize our cash flow to make strategic investments to drive future growth while also retaining the liquidity to continue returning cash to our shareholders over the long-term.

Turning now to capital expenditures, full-year spending totaled \$80 million. Of that amount roughly half was deployed toward the opening of new stores, store remodels and refurbishment. The remaining half was utilized for technology and infrastructure initiatives including our new point-of-sale system.

We anticipate a similar level of spending in fiscal 2015 which includes investments in stores and technology that are designed to maximize our real estate portfolio and facilitate our 1 Pier 1 omni-channel strategy. As Alex mentioned based on the strong trajectory of e-commerce we are leasing space and opening a second fulfillment center in Columbus, Ohio which is expected to come online this fall.

Now I will turn to our outlook for fiscal 2015. We are planning for significant growth in sales, EBITDA and earnings per share. We expect to achieve comp store sales growth in the mid-single-digit range, comparable Company sales growth which includes e-commerce in the high single-digit range.

SG&A expense to be relatively flat as a percentage of sales to fiscal 2014, EBITDA growth in the range of 11% to 17%; earnings per share in the range of \$1.16 to \$1.24 utilizing a diluted share count of 96 million which represents year-over-year growth of 15% to 23%. And additionally for modeling purposes you should assume interest expense of approximately \$11 million and an effective annual tax rate of 39%.

As always our goal is to deliver profitable growth while continuing to make investments that will sustain growth well into the future. Striking that balance allows us to create shareholder value over the long term. I will echo Alex's sentiment and express my appreciation to all of our associates for the dedication and commitment they demonstrate day in and day out. Now I will ask Laurel to open the call for questions.



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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions). Budd Bugatch, Raymond James.

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### Budd Bugatch - Raymond James & Associates - Analyst

Thank you for taking my questions. I just want to make sure I understand the definitions, Cary, since we are seeing some new definitions of total comparable-store sales or comparable-store sales and total comparable Company sales -- make sure what is the base of comparable Company sales, how do we define that?

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### Cary Turner - Pier 1 Imports, Inc. - Senior EVP & CFO

Basically it is going to be the comp store sales and the e-commerce business now that we have the two full years of the business in the e-commerce business.

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### Budd Bugatch - Raymond James & Associates - Analyst

And e-commerce in the fourth quarter, did you give that number? I know you had it for the year at 4% earlier didn't you say it was 5%?

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### Cary Turner - Pier 1 Imports, Inc. - Senior EVP & CFO

Correct.

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### Budd Bugatch - Raymond James & Associates - Analyst

So it's 5% for the fourth quarter and can you give us a dollar number for the year?

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### Cary Turner - Pier 1 Imports, Inc. - Senior EVP & CFO

I would have to get back to you.

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### Budd Bugatch - Raymond James & Associates - Analyst

Okay. And I want to make sure on the SG&A I understand for the fourth quarter what were the components of it? I may have missed the bonus reversal or the short-term incentive plan, how much was that or how did that affect the SG&A in the fourth quarter?

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### Cary Turner - Pier 1 Imports, Inc. - Senior EVP & CFO

Well, it wasn't necessary the reversal; it was more of that we only paid out a very small portion of it so that was a benefit to SG&A.

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### Budd Bugatch - Raymond James & Associates - Analyst

And did you quantify that, could you (multiple speakers)?

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**Cary Turner** - Pier 1 Imports, Inc. - Senior EVP & CFO

Last year it was a much bigger piece.

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**Budd Bugatch** - Raymond James & Associates - Analyst

And how did it compare year-over-year then?

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**Cary Turner** - Pier 1 Imports, Inc. - Senior EVP & CFO

It was significantly down.

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**Budd Bugatch** - Raymond James & Associates - Analyst

Can you give us any quantification of that?

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**Cary Turner** - Pier 1 Imports, Inc. - Senior EVP & CFO

Call it \$8 million to \$10 million.

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**Budd Bugatch** - Raymond James & Associates - Analyst

All right, thank you. And on gross margin for next year you talked about SG&A being flat. How should we think about merchandise margin or the components and you have got 30 new stores, 25 that you are giving up, so a net new of five. And the new occupancy, how will that look for the year in -- the new year?

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**Cary Turner** - Pier 1 Imports, Inc. - Senior EVP & CFO

Like I said we are really trying to get everyone focused on gross profit as a percent of sales because there are so many moving parts between margins and occupancy.

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**Alex Smith** - Pier 1 Imports, Inc. - President & CEO

I think, Budd, we can't split that out and it becomes too difficult, but directionally I can tell you that if we look at the merchandise margin just in the stores we expect to see some improvement there over our Y.

So that will be a plus to the merchandise margin. But of course the merchandise margin for the e-com business, which has got the fulfillment cost in there, is going to drag the overall number down.

So you really don't get a clear picture just looking at the merchandise margin at a total Company level, but we are expecting to have a lower markdown percentage as a percent of sales and we are going to manage very, very carefully our promotional discounts.

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**Budd Bugatch** - *Raymond James & Associates - Analyst*

And I understand, Alex, your interest -- and Cary, your interest in getting people to focus on the overall margin. But you do report occupancy and buying as a separate line item and are you going to continue to still do that?

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

Yes, so for rough numbers take occupancy up some \$12 million (multiple speakers).

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**Budd Bugatch** - *Raymond James & Associates - Analyst*

If I was right in the fourth quarter, if my math was right for your \$73.2 million in the merchandise margin with the competitive set got to around 55.8%, is that about right?

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

That is about right, but remember, it was primarily due to additional promotion, but more importantly to the increased clearance to get rid of the seasonal goods.

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**Budd Bugatch** - *Raymond James & Associates - Analyst*

I understand. Did you quantify that at all or would you be willing to what that impact might have been?

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

No.

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**Budd Bugatch** - *Raymond James & Associates - Analyst*

Okay. I will let others go on. Thank you very much for taking my questions.

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**Operator**

David Berman, Berman Capital.

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**David Berman** - *Berman Capital - Analyst*

Hi, guys. I am pleased to see a bit of stabilization there in the sales of the weather. That is good news. I wanted to focus on the Internet for a second. You just mentioned in the previous questioning that it was 5% of your business in the last quarter, and I think it is going to be 10%. That is the goal at the end of 2015; that is correct, yes?

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**Alex Smith** - *Pier 1 Imports, Inc. - President & CEO*

Yes.

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**Cary Turner** - Pier 1 Imports, Inc. - Senior EVP & CFO

2016.

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**David Berman** - Berman Capital - Analyst

So what percentage growth rate -- I understand it is a low base, but what percentage growth rate you are expecting? Are you running at like 90%, 100% right now, 80%, 90%, 100%?

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**Alex Smith** - Pier 1 Imports, Inc. - President & CEO

Yes, we expect our e-com business to at least double this year.

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**David Berman** - Berman Capital - Analyst

Is that the run rate that you have been seeing in the last quarter? I don't know if you mentioned that. Forgive me.

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**Alex Smith** - Pier 1 Imports, Inc. - President & CEO

Oh, yes.

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**David Berman** - Berman Capital - Analyst

And what are you seeing, if you can embellish a little bit more on the type of products that are doing well? Also, talk a little bit about what you expected to do well, what didn't do well and what did do well, like what are you learning about that?

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**Alex Smith** - Pier 1 Imports, Inc. - President & CEO

Well, and I think we have talked a little bit about this before. We are seeing over-indexing on some departments. The two standouts are our rug departments and our curtain departments where the percent of e-com business is significantly higher than the percent of store business. And there are others that over-index, and there are some departments, particularly the low ticket pickup products which slightly under-index. So we are seeing our online business is more geared towards higher average unit retail than our store business.

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**David Berman** - Berman Capital - Analyst

And in terms of the margins are the products that are doing well higher or lower margins? What is the profitability like? And related, what is the profitability like for the Internet?

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**Alex Smith** - Pier 1 Imports, Inc. - President & CEO

The profitability is just fine. In fact, we sell a little less clearance online than we sell in the stores, so the overall sort of blended merchandise margin before the fulfillment centers is a little bit higher than the stores.

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**David Berman** - Berman Capital - Analyst

Right, right. And the profitability, the margins, can you quantify any numbers for us in terms of the contribution margins to the business?

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**Alex Smith** - *Pier 1 Imports, Inc. - President & CEO*

Not really. I think what I would just like to do is just sort of reemphasize the point that I made in the prepared remarks, which is this is early days. We still haven't got the full benefits of a large-scale business, but we are already certain that the profitability of our online business will be at least -- and I want to kind of underline at least -- as profitable as our store business. Now, I think that's -- considering that our stores are so profitable, I think that is a pretty important thing to think about.

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

(Technical difficulty) because of all of that we are agnostic as to which channel she decides to shop on and we will get the profitable sales through both channels.

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**David Berman** - *Berman Capital - Analyst*

Okay. All right, well, good luck in that, guys. Thanks a lot. Good luck.

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**Operator**

Alan Rifkin, Barclays.

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**Alan Rifkin** - *Barclays Capital - Analyst*

So certainly the effects of the weather are certainly well documented. But maybe, Alex, can you shed a little bit more color on exactly why you are pushing out your three-year goals?

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**Alex Smith** - *Pier 1 Imports, Inc. - President & CEO*

I think it is really just a re-basing of the numbers, Alan. There is nothing sinister in it, there is no frankly deep thought in it. It is just we ended last year where we ended it and so we just thought it prudent to just move them out a year. But I wouldn't read anything of great significance into that. We just wanted to make sure we had updated everybody on our three-year plan.

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

Alan, right now we are at \$202 a square foot and we think it is going to take -- maybe we can get there sooner than the end of fiscal 2016, but for now I don't want people building a model that says we get there this year.

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**Alan Rifkin** - *Barclays Capital - Analyst*

Right. Although two successive years of mid-single-digit comps should take you from \$202 to \$225 in two years, is that the right thinking?

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

That is where we are.

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**Alan Rifkin** - Barclays Capital - Analyst

Right, okay. Cary, on the gross margin line of the approximate 320 basis point decline that is not occupancy, how is that broken down between heightened promotions and the e-commerce effect?

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**Cary Turner** - Pier 1 Imports, Inc. - Senior EVP & CFO

We didn't break that out.

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**Alan Rifkin** - Barclays Capital - Analyst

Okay. Is there any estimate on your part as to when e-commerce will no longer be dilutive to gross margins? If you hit your 10% e-commerce goal will gross margins still be deteriorating in that?

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**Cary Turner** - Pier 1 Imports, Inc. - Senior EVP & CFO

I think we will get a little bit closer and as we see what happens with this year and next and we see efficiencies that we expect to get as we get scale we will be able to give more clearer numbers.

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**Alan Rifkin** - Barclays Capital - Analyst

Okay. And just one last question if I may. You folks pointed out the adverse effect in your key markets in the two-thirds of the days. How many stores in total are in these key markets that you define as that?

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**Alex Smith** - Pier 1 Imports, Inc. - President & CEO

I don't think we defined key markets. I think what we said was 75% (inaudible). What we said was 75% of our quarter four trading days were impacted in some way. So we get a lot of stores everywhere, so many markets are key markets for us and all of them got blasted.

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**Cary Turner** - Pier 1 Imports, Inc. - Senior EVP & CFO

And to reiterate, when we look at the business in California and Florida we saw mid-single-digit comps.

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**Alan Rifkin** - Barclays Capital - Analyst

Okay, that is what I was looking for.

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**Alex Smith** - Pier 1 Imports, Inc. - President & CEO

(technical difficulty) what you were looking for.

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**Alan Rifkin** - Barclays Capital - Analyst

Okay, thank you all very much.

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**Operator**

Anthony Chukumba, BB&T Capital Markets.

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**Anthony Chukumba** - *BB&T Capital Markets - Analyst*

I had a question in terms of the guidance. So the \$1.16, the \$1.24, it's based on a fully diluted share count of 96 million shares. So I mean, but you've already repurchased \$90 million of stock so far quarter to date. So am I right to assume that essentially you are envisioning that \$1.16 to \$1.24 assumes no additional share repurchase activity for the remainder of this year?

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

Correct.

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**Anthony Chukumba** - *BB&T Capital Markets - Analyst*

Okay. I just wanted to clarify that. All right, thanks (multiple speakers) guys.

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

That is just for modeling purposes and we will continue to update people as the share count changes.

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**Anthony Chukumba** - *BB&T Capital Markets - Analyst*

Okay, that is helpful. Thank you.

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**Operator**

Adam Sindler, Deutsche Bank.

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**Adam Sindler** - *Deutsche Bank - Analyst*

Good morning. I hope everyone is doing well. A couple of questions. Cary, one, just a couple housekeeping. On the SG&A flat as a percent of sales comment, that is only expenses excluding D&A, correct?

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

Yes. The D&A is a separate line item.

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**Adam Sindler** - *Deutsche Bank - Analyst*

Right, okay. But I just wanted to make sure because sometimes you report the total expense number. And then on the flat SG&A, is higher incentive comp a big piece of that? And then I guess the follow-on is what else would potentially drive flat SG&A on a high-single-digit brand comp?

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**Cary Turner** - Pier 1 Imports, Inc. - Senior EVP & CFO

So we are going to see variable expenses being leveraged, especially store payroll and other store-related expenses. And then the relatively fixed expenses with that there will be some deleveraging, but net-net in total, total SG&A will be flat to slightly better.

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**Adam Sindler** - Deutsche Bank - Analyst

Okay, but just on the deleverage of the fixed, is that because of further investments in e-commerce or simply a more conservative outlook given sort of the run rate over the last several years?

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**Cary Turner** - Pier 1 Imports, Inc. - Senior EVP & CFO

No, it is a continued investment in people, as Alex mentioned, and also the incentive comp piece.

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**Adam Sindler** - Deutsche Bank - Analyst

Okay. And just as e-commerce grows, I know you like to have buying, planning, allocating teams fully staffed as certain categories get to 5%. Is that part of the further personnel growth?

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**Cary Turner** - Pier 1 Imports, Inc. - Senior EVP & CFO

Absolutely. You heard Alex say most of the hiring that we are doing is with e-commerce related activity be it in planning, be it in additional buyers, marketing, etc.

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**Adam Sindler** - Deutsche Bank - Analyst

Got it. Thanks so much, guys. Appreciate it.

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**Operator**

David Magee, SunTrust.

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**David Magee** - SunTrust Robinson - Analyst

Can you tell me what your assumption is regarding the rate of improvement in online conversions given I guess what would drive that this year would be the assortment expansion.

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**Alex Smith** - Pier 1 Imports, Inc. - President & CEO

I won't give you the exact numbers we are planning, but what I would say is when we set this out we can see that we are going to get conversion improvement from probably eight or nine different line items. And some of it is about improvements to the site in terms of, A, additional functionality and, B, just a better user experience so that is a piece of it.

Some of it is going to come from additional SKUs, that is a piece of it. Some of it is going to come from the great work that the stores are doing in terms of creating online orders through the cash wrap PC. That is a piece of it.



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So, it kind of goes sort of on and on in that vein. And that gets us to a conversion rate this year that we think -- in this fiscal year, which we think will be significantly higher than last year.

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**David Magee** - *SunTrust Robinson - Analyst*

Thank you, Alex. Cary, do you plan to have debt on the balance sheet at year end of this next year?

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

Yes.

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**David Magee** - *SunTrust Robinson - Analyst*

And what (multiple speakers)?

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

It will be as we announced with that term loan B.

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**David Magee** - *SunTrust Robinson - Analyst*

Right, right. Okay. Then with regard to the same-store sales number in the quarter being impacted by a pretty big amount by the calendar shift, 500 bps, was there a give back in a different quarter that was sort of an offset?

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

No, the fourth quarter is really the most impacted.

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**David Magee** - *SunTrust Robinson - Analyst*

Okay, so the third quarter wasn't helped by that same variable?

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

No, no.

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**David Magee** - *SunTrust Robinson - Analyst*

Okay, great. Thank you, guys.

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**Operator**

Joan Storms, Wedbush. Brian Nagel, Oppenheimer.



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**Brian Nagel** - *Oppenheimer & Co. - Analyst*

Thanks for taking my questions. Maybe a couple relatively I guess somewhat bigger picture questions. First off, with respect to the shift in longer-term guidance pushing out some of the targets by a year or so, is it easy to identify as we look at 2014 the guidance now versus what the guidance was previously?

How much incremental investment -- what is the actual amount of incremental investment associated with either your online build out or some of the other initiatives that is now in those numbers?

**Alex Smith** - *Pier 1 Imports, Inc. - President & CEO*

Are you talking about the -- I'm sorry, Brian, I am a bit confused. Are you talking about our earnings guidance or our guidance on the three-year plan?

**Brian Nagel** - *Oppenheimer & Co. - Analyst*

Well, I guess both. Essentially you moved your targets out a bit. Is there a piece as we look at 2014 that there is actually incremental spending here in 2014 that wasn't in the guidance when you previously articulated it?

**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

Yes, it is primarily in two places. The fixed SG&A expenses are up more than what we had thought just because of the additional headcount. But the biggest impact is really the depreciation and that is coming through with the capital expenditures that we have spent over the last couple years of \$75 million to \$80 million.

**Brian Nagel** - *Oppenheimer & Co. - Analyst*

Okay. And a second question with respect to taking some debt on here. You guys are doing such a great job with recovery and through that process you have had a very unlevered balance sheet, you have generated a lot of cash. The question is why now? There are discussions with you and the Board; why take on -- again, it is a modest amount of debt, but why take it on now?

**Alex Smith** - *Pier 1 Imports, Inc. - President & CEO*

I think that is very, very simple. When we look at the prospects for Pier 1 and we look at our strategy and we see what we can achieve over the next few years. And then we look at the way we have been valued recently. We just think that buying stock at the current price is a terrific deal for our shareholders and we wanted to take advantage of it. I mean as we have been in the past, we try and be opportunistic about these things.

**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

But I think more importantly, number one, you said it was a prudent amount and, number two, it just gives us a lot more flexibility to be able to invest in people, invest in capital and return the capital to shareholders.

**Brian Nagel** - *Oppenheimer & Co. - Analyst*

Got it. Then one final question with respect to online, as the online businesses continuing to grow and I think response to some of the questions that you talked about the profile of sales, but have you learned anything more about the customer? Who's shopping online? Is it indeed a new customer to Pier 1 or was it someone was shopping your stores may now also be shopping online, any new data there?



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**Alex Smith** - *Pier 1 Imports, Inc. - President & CEO*

Yes, we have tons of new data every day and the answer is it is some and some and some. I think I alluded in my prepared remarks to those customers who shop us online and in-store and some of those are new customers and we have converted them from online only customers to both.

But if you look at our online business in totality, the biggest percentage of our online business is coming from customers who only are shopping us online. As far as we know. I mean 100% match back so the answer is, yes, lots of new customers.

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**Brian Nagel** - *Oppenheimer & Co. - Analyst*

Well, thank you.

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**Operator**

Brad Thomas, KeyBanc Capital.

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**Brad Thomas** - *KeyBanc Capital Markets - Analyst*

Thanks. Good morning, Alex and Cary. Just wanted to follow-up on some of the commentary about the first quarter that you made Alex, talked about the Easter sell through being quicker than what you had seen last year. I think you said you were pleased with the outdoor sell through being on plan.

Just as we think about comp expectations for the first quarter and I assume that just beyond plan with the mid-single-digit guidance. And then from a margin perspective anything that you'd call out in particular for us to look for in the first quarter here?

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**Alex Smith** - *Pier 1 Imports, Inc. - President & CEO*

No, I don't think there is anything in particular. No, not really. I think thank goodness hopefully it is going to be a normal quarter. The Easter shift I think has been good because Easter in April is always better than Easter in March so that is good. And once we are through Easter the calendar actually, hurray, is actually like for like for the rest of the fiscal year.

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**Brad Thomas** - *KeyBanc Capital Markets - Analyst*

Good. And then just one more question on the guidance, Cary. Just as we bridge this the revenue guidance high-single-digits, the EBITDA guidance 11% to 17% and that is with gross margins flattish, SG&A flattish just curious where you are getting leverage to get that better EBITDA growth?

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**Cary Turner** - *Pier 1 Imports, Inc. - Senior EVP & CFO*

It is really with the -- that increase in sales and you will see that it does come down and we do leverage some of the fixed cost like occupancy and depreciation somewhat fixed as well.

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**Brad Thomas** - *KeyBanc Capital Markets - Analyst*

Got you. Thanks so much and good luck.



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**Alex Smith** - *Pier 1 Imports, Inc. - President & CEO*

Okay, thank you very much. I think that is all the questions we got. Laurel, thanks for doing this for us. And we will be back to talk to you all at the end of the first quarter. Thank you.

**Operator**

This concludes today's conference call. You may now disconnect.

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