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BBY - Q1 2021 Best Buy Co Inc Earnings Call

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OVERVIEW:

Co. reported 1Q21 revenue of $8.56b and non-GAAP diluted EPS of $0.67.

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to Best Buy's First Quarter Fiscal 2021 Earnings Call. (Operator Instructions) As a reminder, this call is being recorded for playback and will be available by approximately 11 a.m. Eastern Time today. (Operator Instructions)

I will now turn the conference over to Mollie O'Brien, Vice President of Investor Relations.

Mollie O'Brien - *Best Buy Co., Inc. - VP of IR*

Thank you, and good morning, everyone. Joining me on the call today are Corie Barry, our CEO; Matt Bilunas, our CFO; and Mike Mohan, our President and COO.

During the call today, we will be discussing both GAAP and non-GAAP financial measures. A reconciliation of these non-GAAP financial measures to the most directly comparable GAAP financial measures and an explanation of why these non-GAAP financial measures are useful can be found in this morning's earnings release, which is available on our website, investors.bestbuy.com.

Some of the statements we will make today are considered forward-looking within the meaning of the Private Securities Litigation Reform Act of 1995. These statements may address the financial condition, business initiatives, growth plans, investments and expected performance of the company and are subject to risks and uncertainties that could cause actual results to differ materially from such forward-looking statements. Please refer to the company's current earnings release and our most recent 10-K for more information on these risks and uncertainties. The company undertakes no obligation to update or revise any forward-looking statements to reflect events or circumstances that may arise after the date of this call.

I will now turn the call over to Corie.

Corie Sue Barry - *Best Buy Co., Inc. - CEO & Director*

Good morning, everyone, and thank you for joining us. Before we get into the details of our results, on behalf of all of us at Best Buy, I want to extend our sincere appreciation and gratitude to all those who are on the front lines working to keep us safe or maintain essential services, and we offer our heartfelt sympathy to all those who have lost someone to this virus or who are sick with COVID-19.

Today, we are reporting Q1 revenue of $8.56 billion, which is a decline of 6.3% from the first quarter of last year. Our Q1 non-GAAP earnings per share were $0.67 compared to $1.02 last year. The Q1 non-GAAP operating income rate of 2.9% was down 90 basis points from last year, primarily due to the operational disruptions caused by the pandemic, which Matt will provide more details on later.

This pandemic has changed the way we work, learn, care for ourselves and importantly, connect with each other. Against that backdrop, our purpose has never been more relevant: To enrich lives through technology. It is because of that purpose that we were, in virtually every jurisdiction with a stay-at-home order in place, designated an essential retailer because of the products and services we offer.

I wanted to take a moment to share how Best Buy has been responding and will continue to respond to the crisis we all face. There are scenarios you plan for as business leaders, and then there are events that simply do not have a playbook. This is one of those times, and our leadership team has been responding to events with a focus on keeping our customers and our employees safe while we meet our customers' essential needs. At the same time, we are committed to ensuring that as this evolves, Best Buy is well positioned to thrive in what will almost certainly be a new and very different environment.

On March 22, we proactively moved all our stores to a contactless, curbside-only model, allowing us to safely serve customers and comply with government orders and recommendations. We also halted all in-home installation, repair and consultation services, choosing to leave the product at or near the doorstep. We did this even in jurisdictions where we were not required to because we believed it was the best way at the time to keep our customers and employees as safe as possible.

I am so incredibly proud of our of teams' ingenuity and execution, they seamlessly implemented a new and highly effective operating model in a matter of 48 hours across our entire store base. As a result, we have retained 81% of last year's sales during the last a 6 weeks of the quarter as we operated in the new model. That's 81% sales retention even though not a single customer set foot in our stores. The strong sales retention is a testament to the strength of our multichannel capabilities and the strategic investments we have been making over the past several years. It is also a testament to the Best Buy culture and our focus on the customer experience as the entire organization pivoted to execute and support the new model.

More than ever, we are fulfilling essential technology needs for customers. In mid-March, we began to see a surge in demand for products that people needed as they complied with stay-at-home orders. That demand continued even after we closed our stores to customer traffic. For the quarter, we saw strong sales growth in computing, gaming and small appliances. Like many other retailers, we saw a sales benefit during the last 3 weeks of the quarter as customers undoubtedly chose to spend some of their government stimulus money on the products and services we provide.

As we entered the second quarter, we continued to shift our operating model as we responded to the evolving environment. On May 4, we began welcoming customers back into our stores to shop Best Buy in innovative ways that follow strict social distancing practices and use proper protective equipment.

Specifically, we are offering a new consultation service to our customers in our stores by appointment only. This service allows customers who need to purchase more complex items to schedule an appointment with one of our sales associates at their local Best Buy store, where they can get advice tailored to their specific tech needs. Customers can schedule appointments by phone, online or by simply driving or walking up to a store. We started with approximately 200 stores and now have almost 700, or about 70% of our domestic stores, operating in this way. Most of the remaining stores are still operating in the curbside-only model, and approximately 40 stores remain completely closed, mainly due to our own decision-making criteria regarding employee and customer safety. Customers have responded very positively to this new way of interacting with us in our stores, with 98% of customers surveyed indicating we made them feel safe during the experience. It is very early, but so far, the demand has been highest for our large appliances and home theater categories.

We are also back in customers' homes, providing valuable services like large product delivery, installations and in-home repairs in approximately 80% of U.S. ZIP codes. We are doing this in a new and innovative way, using safety guidelines before, during and after an in-home visit that meet or exceed the Centers for Disease Control and Prevention guidance. The key, of course, is that we are providing options that let customers choose what works best for them. For the foreseeable future, we will likely employ a variety of models using our local-level prowess to customize operations to the local situation. And we will continually evolve those operating models based on guidance from state and local governments as well as our own point of view on the proliferation of the virus and our ability to operate in a way that is safe for our employees and customers.

I want to take some time to talk about our employees, clearly, the company's most important asset. From the very first days of the pandemic, we told anyone feeling sick or quarantined that they would keep their job and paid. We told any employee whose child was home from school that they, too, would be paid. We gave all field employees who were still serving customers or working in our distribution centers a temporary pay increase. And for all others, we paid their normal salaries for a full month as we took the time to determine how to move forward.

Throughout this difficult time of uncertainty and fast-paced change, we have been committed to communicating as often as possible with our employees. This includes conducting surveys on their need for flexibility as well as their feelings on returning to work so we can continue to improve our processes, facilitate the deliberate and measured return to corporate workspaces and accommodate those with preexisting conditions or safety concerns. Likewise, we built the protocols for returning to customers' homes and welcoming them back into our stores jointly with our field employees. We have created a robust feedback loop, and we connect regularly with other field employees to hear how things are going and solicit immediate feedback to challenges they face, iterating the experience as we go. We have also continued our focus on providing crucial employee benefits and resources like those for mental and financial health, recognizing that the circumstances we each face are far more stressful than any of us may fully realize.

Like most companies, we have had to make tough decisions, including those Matt will touch on regarding the ways in which we have cut costs and preserved liquidity to ensure that, at the end of this crisis, Best Buy remains a strong, vibrant company. I personally want to touch on the difficult decision to furlough employees. While we were pleased to retain more than 80% of our revenue while our stores were closed to customer traffic, the fact remains that we did this without a single store open to customers. Given this fact, it is clear that the current models we are operating simply don't require the staffing our stores had before this crisis began.

In that context, on April 19, we furloughed approximately 51,000 domestic hourly store employees, including nearly all part-time employees. We retained approximately 82% of our full time store and field employees on our payroll, including the vast majority of In-Home Advisors and Geek Squad Agents. Additionally, some corporate employees are participating in voluntary reduced work weeks and resulting pay as well as voluntary furloughs. We have done our best to provide these employees with resources and tools to help them navigate a situation that is undoubtedly new to all of them.

In keeping with our view that all of us are in this together, I am forgoing 50% of my base salary, and the members of the Board of Directors are forgoing 50% of their cash retainer fees. Company executives reporting directly to me are also taking a 20% reduction in base salary. The money saved from these temporary pay reductions is being added to the employee hardship fund we established with our founder, Dick Schulze. This fund was initially created for our furloughed employees as a way of providing them emergency funds should they be required.

I would now like to provide an update from a strategic lens. Last September, we hosted an investor update meeting to provide additional insights into our strategy. Despite the disruption and uncertainty related to COVID-19, we remain focused on executing our Building the New Blue strategy. In many ways, our current way of life in our homes, reliant on technology, has only reinforced our belief in our strategic direction. We firmly believe our strategy will uniquely position us over the long term by leveraging our unique combination of tech and touch to meet everyday human needs and build more and deeper relationships with customers.

Many of the capabilities and initiatives we laid out on stage in September are the muscles we are flexing right now. Our multi-year supply chain transformation has been focused on moving facilities closer to our customers and using automation and process improvements to expand fulfillment options, increase delivery speed and improve the delivery and installation experience. This has included significantly improving the buy online, pickup in store experience for our customers. At the same time, we have been innovating and designing digital experiences that solve customer needs across online and physical shopping. As a result, the team was very quickly able to stand up a robust and seamless customer experience for both the curbside pickup process and the new in-store consultation process.

All of this culminated in domestic online growth of 155% for the quarter. And during the 6 weeks we ran our curbside-only model, domestic online sales were up more than 300% compared to last year. Almost 50% of those sales were from customers choosing to pick up their products curbside at our stores. Customer satisfaction scores for the curbside pickup experience remains strong with more than 83% of those surveyed indicating they are extremely likely to recommend Best Buy based on their curbside experience.

As it relates to supply chain, let me say first that since the beginning of the pandemic, we've taken a variety of steps to create the safest possible experience for the employees in our distribution centers while also ensuring that we're still able to deliver to customers with speed.

Additionally, the infrastructure and capabilities we have built to thrive during peak holiday periods is serving us well. Even with the sustained online growth levels of approximately 350% during the last 3 weeks of the quarter, we did not have material disruptions and maintained our levels of fast service.

We will continue to invest in all of these capabilities that focus on the customer experience and that are designed to provide choice, speed and now safety. We will also, of course, continue to bring our deep CE expertise and unique ability to partner with vendors to commercialize their new technology, offering customers great products and solutions. In fact, in Q1, we saw a significant increase in demand for our expanded assortment of digital health and fitness products, including things such as at-home fitness equipment and fitness recovery products that truly empower customers to take care of their own health at home.

We believe that not only will technology innovation continue, it will accelerate as a result of the pandemic. We believe many of the customer behavior changes resulting from this time of stay-at-home orders will continue to exist moving forward. Best Buy and our vendor partners are rapidly adjusting our offerings to support these new needs in areas like video conferencing, food preparation and storage and family entertainment.

Turning to our In-Home Consultation service. In mid-March, we pivoted to provide consultations on a digital basis only. We are proud of the nimble way our team quickly transitioned to this alternative way of interacting with customers, and we're pleased with the number of consultations that took place this way. Because of our investments in the technology backbone, our In-Home Advisors were able to remain productive during this time and continue to provide customers a high level of consultation service. With our Geek Squad, we are in a unique position to help people productively work and learn in their homes.

While overall Q1 interactions with our Total Tech Support customers were down compared to last year as our in-store and in-home services were unavailable, our remote technical support provided a critically stable support solution through these challenging times. In addition, we have cross-trained our Geek Squad Agents to work in our call centers, providing crucial phone and chat support to solve a variety of customer needs. We also utilized our Geek Squad Agents to support our online customer experience by making same-day deliveries to customers' homes from 200 of our stores. As we moved back into homes and welcome customers back into our stores, demand for our services has been very high.

Turning to Best Buy Health. Our focus on health, in particular helping seniors live more independently with our unique combination of tech and touch, has become even more relevant as the world responds to the COVID-19 pandemic. In Q1, to support our base of over 1 million seniors, we moved quickly to adapt our operations so our caring center agents could support more than 150,000 calls each week while complying with stay-at-home orders. The time spent by our agents on the phone with our customers was above the normal average at over 9 minutes per call in many weeks as we took the time to ensure we are answering questions and addressing requests to our fullest ability. Our service during this period averaged an NPS of 80, and we are incredibly proud of our caring center agents and the empathy with which they serve this vulnerable population, especially during this time.

We also had the opportunity to help our commercial partners manage through this time with the help of technology. A recent example is Holiday Retirement, a leading senior living community where 29,000 residents have been outfitted with our Lively Mobile Personal Emergency Response, or PERS, devices. These devices provide access to our emergency response service at the press of a button. We worked with Holiday to leverage these devices to efficiently broadcast timely information and protocols related to COVID and shelter-in-place to the senior residents.

Lastly, we continued to build out our capabilities as we execute our long-term health strategy. Data is an essential currency of this strategy, and we recently entered into an important partnership on that front. Validic is an industry-leading technology platform that aggregates data from everyday connected devices in the home, processes it and then provides meaningful insights. Together with Validic, we are bringing to market innovative remote monitoring solutions to better manage chronic health conditions in the home.

In conclusion, we entered the year with financial and strategic momentum and a strong balance sheet. We have a suite of assets that allow us to uniquely and safely serve our customers in whatever way they choose, whether that's curbside pickup, free next-day shipping, remote technical advice and support, virtual consultations, in-store appointments, in-home installation or doorstep delivery. We know customers and employees will have different shopping expectations anchored in safe environments and processes. We hope to set the standard for safe retailing by constantly adapting our model, leveraging and building on our unique suite of assets.

The environment continues to evolve. And while there are many models and a great deal of speculation, there is still a high level of uncertainty at both the micro and macro level. With that said, we are scenario-planning in a way that addresses a number of variables. First, meaningful unemployment will almost certainly be with us through the fiscal year, not necessarily at the level we are seeing now, but enough to likely have downward macroeconomic effect. Second, it will be important for us and any retailer to have a flexible enough operating model to accommodate the possibility that some states will continue to relax restrictions while others, at the same time, may find themselves needing to tighten similar restrictions on how consumers engage with each other and local businesses. Finally, we will continue to prioritize customer and employee safety, advocating for preventative measures such as social distancing and masks for both customers and employees. It is our belief that these measures will continue into the foreseeable future and will allow us to do what we promised at the very beginning of this crisis: Be there for our customers in as many ways as possible while ensuring customers and our employees remain as safe as possible.

As challenging as the current situation is, I am certain Best Buy will remain a strong, vibrant company that is well positioned to deliver on our purpose and thrive in a new and different environment. In fact, we have taken the opportunity to move faster as this environment accelerates changes in the ways customers want to interact with retailers. For example, we were already preparing to roll out curbside service, store consultations and certified cross-training of employees. As such, the implementation of these capabilities is not just a response to the pandemic. They are in fact an acceleration of our existing strategy.

Lastly and very importantly, I want to take this moment to thank the thousands of employees that have made this all possible. They have faced immense change with grit, determination and compassion and have helped us shape our approach to safe retailing. Many are working with customers every day, some of whom are also scared, frustrated and occasionally hostile in this COVID environment, to ensure they have access to the products and services they need to work, learn, entertain and connect from home. Others are working tirelessly to maintain a supply chain that delivers with speed and keeps our customers at home, and so many employees are making technical and operational changes every hour from their home office. None of this is possible without their dedication, and I am truly grateful and feel lucky to be on the team with them.

Now I would like to turn the call over to Matt for more details on our Q1 financial results.

Matthew M. Bilunas - *Best Buy Co., Inc. - CFO*

Good morning. As Corie described, the pandemic has dramatically changed how we interact with our customers. We are thoughtfully approaching each decision, balancing the safety of our employees and customers while creating long-term value for our shareholders. Even with the outstanding execution from our employees and the strong customer demand for the essential technology we provide, there is no denying the financial impact the pandemic has had.

In Q1, the stay-at-home orders and changes to our operating model resulted in an immediate and complete channel shift that put near-term pressure on our operating income rate. Online revenue was up more than 155% year-over-year and was 42% of domestic revenue compared to 15% last year. In a typical quarter, the operating income rate in the store and online channel are very similar as we find the lower gross profit rate online is offset by lower SG&A as a percentage of sales compared to our store channel.

In Q1, our Enterprise gross profit rate was approximately 70 basis points lower than last year as we incurred higher supply chain cost to fulfill the online sales. In addition, while we took numerous steps to control cost and manage profitability in the quarter, we continued to incur the majority of the cost to run stores, including payroll and rent. In fact, we continued to pay our field associates, in some cases at a higher rate, through most of the quarter. Therefore, we did not see the SG&A leverage we would expect with a more gradual shift of sales between channels. As a result, our enterprise non-GAAP operating income rate declined 90 basis points was driven by both a lower gross profit rate and an unfavorable SG&A rate compared to last year.

Before I talk about our first quarter results in more detail, let me start with a reminder that on March 21, we withdrew our fiscal '21 guidance for both the first quarter and the full year due to the uncertainty related to the potential impacts associated with COVID-19 pandemic.

I would now like to provide additional details on our results versus last year, starting with how sales trended during the quarter. As we reported in our April 15 press release, our enterprise revenue was up 4% year-over-year for the first 7 weeks of the quarter ended March 20. This was ahead of our original expectations as in mid-March, we began to see the surge in demand for products that people needed to work or learn from home as well as gaming products. In fact, during the 8 days ended March 20, our enterprise revenue grew approximately 25% year-over-year.

While we continue to see heightened demand for these products, we materially changed our operating model and therefore we began to experience overall revenue declines. As a result, in the first 3 weeks of the new model, from March 21 to April 11, revenue declined approximately 30% compared to last year. In the last 3 weeks of the quarter, from April 12 through May 2, sales trends improved as stimulus funding began to circulate. As a result, during that time period, revenue declined approximately 8% compared to last year.

In our domestic segment, revenue for the total quarter decreased 6.7% to $7.9 billion. The decrease was driven by a comparable sales decline of 5.7% and the loss of revenue from 24 large-format stores that were closed in the past year as part of our normal course of business. Our comparable sales calculation includes revenue from all stores that were temporarily closed or operating in our curbside-only operating model during the period as a result of COVID-19.

From a merchandise perspective, as Corie mentioned, we saw growth in our computing and gaming categories. This growth was more than offset by declines in home theater, mobile phones and digital imaging. In addition, comparable sales in the services category declined 16%. The decline in services was primarily due to store closures and the corresponding higher mix of online sales, which has a lower attach rate than in-store as well as the fact that we suspended in-home services midway into the quarter.

In our international segment, revenue decreased 2.1% to $647 million, primarily driven by approximately 320 basis points of negative foreign currency impact, which was partially offset by revenue from new stores opened in Mexico in the past year. Our international comparable sales were essentially flat to last year even though all stores in Canada were closed to customer traffic for approximately 40% of the quarter, similar to the U.S.

Turning now to gross profit. The domestic gross profit rate declined 70 basis points to 23%. As I stated earlier, the decrease was primarily driven by supply chain cost associated with the higher mix of online revenue. We also saw lower profit sharing revenue from our credit card arrangement and product mix pressure, but these impacts were largely offset by lower promotional activity across multiple categories.

The impact from the lower profit-share revenue was approximately 20 basis points compared to last year. We expect to see continued pressure from lower profit-sharing revenue related to our private label and co-branded credit card arrangement as the economic ramifications of COVID-19 are expected to lead to higher credit card defaults over time. The international gross profit rate decreased 190 basis points to 22.3%, primarily due to lower year-over-year gross profit rate in Canada, the result of a lower mix of higher-margin services revenue and higher supply chain costs.

Moving to SG&A. Domestic non-GAAP SG&A decreased $101 million compared to last year. And as a percentage of revenue, SG&A increased approximately 10 basis points to 19.7%. The largest driver of the expense decline was lower incentive compensation expense of approximately $70 million. The majority of this was related to short-term incentive compensation as we did not pay or accrue bonuses for first quarter performance. We also incurred lower store payroll expense due to the Federal CARES Act employee retention tax credit.

As Corie stated, we continued paying all of our store associates through April 18 whether they were working or not, and we paid hourly incentive pay to employees who were working in our stores and distribution centers. We also incurred additional costs, such as safety measures and supplies, associated with actions we took in response to the pandemic. In the quarter, we incurred approximately $200 million of costs related to our COVID-19-related actions or approximately $131 million when including the employee retention credit of $69 million. This employee retention credit is a payroll tax credit for approximately 50% of qualified wages and health benefits paid to retained employees not working as a result of COVID-19.

On a non-GAAP basis, the effective tax rate of 27.2% compared to 20.1% last year. The increase versus last year was primarily driven by a decrease in the tax benefit from stock-based compensation. Our enterprise non-GAAP diluted EPS of $0.67 includes a negative $0.07 per share impact from the higher tax rate and a negative $0.02 per share impact from higher net interest expense, partially offset by a $0.03 per share benefit from the net share count change.

During the first quarter, we returned $203 million to shareholders through $141 million in dividends and $62 million in share repurchases. As we previously communicated, we suspended share repurchases on March 21. We have taken and are taking a number of additional actions to bolster the balance sheet and provide flexibility, including drawing the full amount of our $1.25 billion credit facility on March 19. Other actions include: Lowering merchandise receipts to match demand, which resulted in a 23% decline in our Q1 ending inventory balance compared to last year; reducing promotional and marketing spend to align with our temporary operating model; and suspending our 401(k) company matching program.

From a capital expenditure standpoint, we are reducing our spend to focus on mandatory maintenance or high-value strategic areas. When we entered the year, our outlook we shared was to spend between $800 million and $900 million in capital expenditures during fiscal '21. We now expect to spend in the range of $650 million and $750 million. We remain committed to spend in areas such as technology, automation and our health strategy. We are deferring spend in areas like store remodels, and we are reducing the number of stores receiving electronic sign labels this year.

As a result of the ongoing uncertainty related to COVID-19, we are not providing financial guidance at this time. However, I would like to provide some insight into how we are thinking about Q2 and the rest of the year.

Our priority has been and will continue to be the safety of our employees and customers while providing essential products and services. We are focused on managing our profitability and liquidity, balancing our short-term decisions to navigate this unprecedented situation while preserving the elements of our strategy that will ensure we remain a vibrant company in the future. For the remainder of the year, there are many factors we are continuing to weigh, including: One, the depth and duration of the pandemic; two, the impact of current to potential future government stimulus actions; three, the impact to consumer and growing unemployment; four, the evolution of our various operating models; and five, how and where our customers are choosing to interact with us.

It is difficult for us, or anyone else for that matter, to model how long this continues and the extent to which the economy moves into a prolonged recession. In the first 2 weeks of Q2, we have retained approximately 95% of sales compared to last year. We would expect that our Q2 sales growth rate will likely continue to be pressured throughout the quarter. We also expect that our online sales will continue to be high as a percentage of overall sales in the second quarter, which will continue to pressure the gross profit rate. While we do expect to see payroll -- lower payroll and short-term incentive costs, we will continue to have some costs associated with a longer-term operating model, such as store rent expense, and continued rate pressure from lower profit-sharing revenue related to our credit card arrangement. Therefore, we still expect our Q2 operating income rate will decline on a year-over-year basis.

Lastly, as Corie mentioned, we will likely employ a variety of operating models during the second quarter, all adapted to the local market conditions and emphasizing safety for our customers and employees. To the extent we are able to increase the level of customer traffic in our stores by expanding hours or opening some stores beyond our current appointment-only model, we may reduce the operating income rate pressure by expanding gross margins and further leveraging SG&A.

I will now turn the call over to the operator for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We will now take our first question from Greg Melich from Evercore ISI.

Gregory Scott Melich - *Evercore ISI Institutional Equities, Research Division - Senior MD*

Great job, all of you, pulling this all together. I'd love to dig a little more into the supply chain and the inventory down 23%. Could you go into a little bit more on which categories you've been able to secure products? And which ones that you think it might be more challenging, particularly as we think about back-to-school in a couple of months.

Matthew M. Bilunas - *Best Buy Co., Inc. - CFO*

Sure. I'll start and then maybe Mike can jump in. I think overall, we think that the teams did an amazing job balancing the inventory through the quarter. We've clearly had a number of different sales trajectories through the quarter. So in the quarter, we likely saw some constraints in some key areas, such as computing and gaming, but we were able to manage through that quite well. I think overall, we're pleased with the way the teams managed through the inventory. And as we look into Q2, I would say we'll continue to see a little bit of constraints going into the quarter, but likely nothing to the impact that we saw in Q1.

Mike, I don't know if you'd add anything.

R. Michael Mohan - *Best Buy Co., Inc. - President & COO*

Yes. Thanks, Matt. And Greg, thanks for the question. And maybe just a little bit of backdrop. Before the pandemic started, we were dealing with the tariff situation from last year, and so our teams have been working tirelessly around countries of origin and our sourcing from all of our partners. And I felt really good as we entered the year as to where we were from an inventory position.

Some of the categories that saw the demand spike. Freezer saw demand spike. Some network equipment saw demand spike. Some of the computing products, monitors, things that you would actually need to work more from home or learn from home, were the ones that got constrained and the ones that we're working the fastest to be back in stock. Based on what we have visibility to and work with our top partners, we feel really good about our inventory position from here going to the balance of the quarter.

We now have to plan a back-to-school during a back -- during a pandemic, which is also new to all of us, too. But I feel good where we're at with the work with our partners.

Gregory Scott Melich - *Evercore ISI Institutional Equities, Research Division - Senior MD*

If I could just follow-up on that, what would be the ideal amount of inventory? I mean, was any of that reduction just because sales were down? Or was it really just getting the supply? Would you like inventory to be flat year-over-year?

Matthew M. Bilunas - *Best Buy Co., Inc. - CFO*

Yes. I think it's a balance. To answer that question, we clearly reduced inventory to match the sales trajectory, but we also wanted to make sure we refined the inventory for the products that were in high demand, like computing. And so you tend to look for areas that aren't -- where the sales trajectory is not as high and you right-size as much as you can and continue to find the products that are in high demand. So ideally, we would like to have more computing in some -- more inventory in some areas because we probably could have seen more sales if -- had we had it, is the answer.

Operator

We will now move to our next question from Karen Short from Barclays.

Karen Fiona Short - *Barclays Bank PLC, Research Division - Research Analyst*

Congratulations, obviously, on working through very volatile times.

Corie Sue Barry - *Best Buy Co., Inc. - CEO & Director*

Thank you, Karen.

Karen Fiona Short - *Barclays Bank PLC, Research Division - Research Analyst*

So I just wanted to ask a little bit on, I guess, the reintroduction of services. I guess could you give a little color on the demand you're seeing for IHAs and also total tech support? Because I guess there's 2 sides of the debate, which is: One, that pent-up demand got pulled into 1Q; but then the other side of it is people couldn't do wholesale like home office reconfigurations just beyond a replacement laptop or printer, I mean, more complicated types of overhauls. So if you could give a little color on that. And then I had another follow-up.

Corie Sue Barry - *Best Buy Co., Inc. - CEO & Director*

So I'll try to give a little color on both TTS and IHA. So we talked about it a bit in the script. We did definitely see some usage, but the majority of it was remote or via chat and call because, obviously, you couldn't come into the stores and we couldn't go into your homes. And so not only were we constrained by a bit of what you were talking about, Karen, which is you could only put so much of your home office together, we were also just constrained by the way we were operating.

And I think we've talked about this before, this severe of a channel shift makes service sales harder than when we have our stores open and we have a chance to provide that service. We are definitely seeing pent-up demand as we start to open up our stores to the appointment model. Many of the appointments being made are people who want to come in and bring, especially as you can imagine, home office or phone products in for us to help take care of them. And we can also see that as we're going back into people's homes, where the demand and the request for us to come to their homes to fix things like refrigerators, laundry, that has been very high. And so I think there is definitely pent-up demand there as we're heading into Q2, and the team is finding new ways to serve that.

On the IHA side of things, it was very interesting. The team across all of our in-home businesses had been very flexibly trying to serve customers either digitally, phone, chat, any way that they can. They moved -- IHA moved to digital consultations in mid-March. Our IHAs are also helping with this really heavy volume of inbound sales calls and chats. And they are also helping with the new in-store consultation model. Before you come to the store, we actually have a pre-call. And our In-Home Advisors, in some cases, are helping with that pre-call because we can really figure out what it is that a customer needs.

I will say, if I just were to give a call data points, in April, we saw our IHA business was actually up, and over 60% of that was coming from chat and digital channels. And that through those channels, those virtual consultations, was at a 91 NPS. So this idea that we can more flexibly use the in-home resources, not just physically in people's homes, but in a more virtual consultative way is really, really interesting and something that I think will be a muscle we continue to flex as we go forward.

Karen Fiona Short - *Barclays Bank PLC, Research Division - Research Analyst*

Actually, that leads into my next question. I mean, looking at your very strong retention rates that have only gotten better, but also pairing that with the e-com now at 42% of sales. I guess I'm wondering how you think about evaluating the physical store base going forward just more broadly.

Corie Sue Barry - *Best Buy Co., Inc. - CEO & Director*

Yes. I would start with -- our stores are absolutely an asset, and they have been an asset throughout this. And I'll just use a data point in April. 65% of what we sold online, which is the vast majority of what we sold, was either picked up curbside or shipped from a store. And so this asset of the store base is very real. Now you can imagine what we're discerning is how might the stores look and work differently in the future, and how might they provide a variety of fulfillment options, a variety of service and high-touch consultative options? Like this opens a lot of doors for how your stores might work differently, and that's where our focus is at this point.

Operator

We will now take our next question from Curtis Nagle from Bank of America.

Curtis Nagle from Bank of America, please ensure you are not on mute. We currently can't hear you.

Curtis Smyser Nagle - *BofA Merrill Lynch, Research Division - VP*

Apologies, I was on mute.

Corie, maybe just quickly just digging back into the point on sales in May so far. So down I guess about only 5%, that is an acceleration. Really, really impressive numbers. Would you be able to talk about what's driving that? Is that further acceleration in online, better curbside? I mean, what's going on there?

Corie Sue Barry - *Best Buy Co., Inc. - CEO & Director*

I'll start, and then maybe Matt can add more color because I'm sure I'll miss something. I think there's a lot that's going on there. So curbside, even if you look at the original retention we announced at the beginning of curbside, which is around 70%, you can tell that accelerating because by the end of the quarter, we were already at 81%. And so just the -- I think the performance, overarching, we have curbside, the teams were amazingly creative and thoughtful about how they implemented that and definitely got better and better and better at providing that service.

We also were very clear, the stimulus dollars that started to flow toward the end of the quarter were absolutely helpful. And those, I would strongly believe, are carrying into Q2 here. Not all the checks have yet been distributed, although the vast majority now of that money is out there. But we definitely see that stimulus starts buoying the level of demand.

And then I think people continue to have more needs as they spend more and more time in their homes. Like the initial demand pull was definitely around working and learning from home. And this new appointment model, what we're starting to see is there is also demand for cooking. And importantly, I think we all feel it, entertaining at home and creating new and different entertaining cases, like what we see in gaming. And so I think there is also that once you layer on a little bit of a point [we do it all], you also start to see various demand for some of the other aspects of what it means to be sheltering in place at this time.

Matt, I don't know if you had anything to add?

Matthew M. Bilunas - *Best Buy Co., Inc. - CFO*

No, I would say -- I think just in general, too, as we become more proficient in our model, that customers are more comfortable as they engage with us, I think there's a general improvement in our execution and just how customers are learning how to shop in this new environment.

Corie Sue Barry - *Best Buy Co., Inc. - CEO & Director*

Yes. I think that's a really good point, and I would just lift up. Our teams have done an amazing job on awareness on how to shop. If you go to our website, we have literally a whole site that just walks through all the different ways in which you can interact with Best Buy and then what's applicable depending on your geography. And you can imagine, that's going to take some time for our customers to understand and actually have awareness of all the different ways they can shop Best Buy.

Curtis Smyser Nagle - *BofA Merrill Lynch, Research Division - VP*

Got it. That's very helpful. And then maybe just a quick one. And perhaps this is a bit early to comment on. But could you talk a little bit about some of the changes you might be making in terms of your in-store product assortment to maybe better cater to people living and staying in their homes more? You'd mentioned health products or fitness products as an example. Yes, how could the stores change over the kind of the coming months and years going forward?

R. Michael Mohan - *Best Buy Co., Inc. - President & COO*

Curt, it's Mike. I'll start and then Matt or Corie can chime in. We look at the customer demand signals all the time. And what I think is interesting during this pandemic, the idea of where we're trying to play, and I'm going to be specific to health, we've always had an insight that knowledge should be playing a strong role in helping enrich people's lives, and that was the predisposition around the acquisition of GreatCall, how we thought about that space.

And as people are really thinking about what else they should or could we doing at home, things in that space definitely have popped. It's still a small business for us, but that's going into the fitness category last year. It was -- now, there's been significantly more demand, but -- in things like oxygen sensors, thermometers and things that you would want to do to just to check and maintain your health are becoming more important because those devices, while they serve a need, are now starting to connect to other things consumers are highly interested in, which I think bodes extremely well for Best Buy.

The gaming resurgence was a bit of a surprise. I'll be candid. Everyone had thought the gaming category was going to wait for this fall for the new console resets. But clearly, if you have kids at home and you cannot be the best teacher in the world, a substitute has become a Nintendo Switch or an Xbox or a Playstation. And that's new demand, and we think that demand will actually buoy into stronger demand as the year progresses with new devices.

The category that I'm intrigued about as we get back to people working with us, whether we're going into their homes, so we intend to go back into people's homes with IHAs in early June, but as people come to our stores for consultations, is people thinking about how to update the way they prepare food and store it and how they're thinking about entertainment. So the categories that we're really good at, these complex, highly consultative sales. I think there's some good opportunity, and our assortments there may be more curated, but also serving customers' needs more specifically as they look for doing different things.

Matt or Corie? [Anything you guys?]

Corie Sue Barry - *Best Buy Co., Inc. - CEO & Director*

The only thing that I would add is to build on Karen Short's question just a little bit. I think the complex, full home office and learning solutions will also continue. I think people have been piecing together kind of what they can to make it work. As I believe work from home becomes a more sustainable practice, I think these more fulsome approaches to home office will be really important.

Operator

We will now take our next question from Scott Ciccarelli from RBC Capital Markets.

Scot Ciccarelli - *RBC Capital Markets, Research Division - MD & Consumer Discretionary Sector Analyst*

Scott Ciccarelli. You guys talked about getting a benefit from the stimulus checks. That makes sense. I think a lot of companies did. But do you have any way to estimate the amount of pull-forward demand you may have benefited from in the quarter as we try and kind of think about the balance of the year?

Matthew M. Bilunas - *Best Buy Co., Inc. - CFO*

Yes. I can start and then either Mike or Corie can jump in. I think we actually don't believe there was much pull forward into the quarter. I think if you think about the types of products we were selling, there's a continued, sustained demand that we're seeing. I think people's lives have also changed in a way that demand that they probably didn't know they had before, they now have in a new world where technology at home is more important. Things like monitors at home that you may not would have bought. So I think we actually think a lot of what we're seeing, or most of what we're seeing, is not pull-forward as much as it is incremental to an otherwise different situation.

Corie Sue Barry - *Best Buy Co., Inc. - CEO & Director*

I think Mike's gaming example is the perfect one, meaning that's not pull-forward demand. That's demand that would not have existed. People would not have bought those gaming consoles. They would have waited for the next generation of consoles to come in December. But because you're in this unique life situation, there's real incremental demand there. And I think that's the perfect example of what we're seeing.

Scot Ciccarelli - *RBC Capital Markets, Research Division - MD & Consumer Discretionary Sector Analyst*

Okay. And then as you talk with your vendors, obviously, you've had a lot of discussions with them, given some of your inventory commentary. Everyone's been on hold, right? So based on what you know at this point, is there any kind of change to, let's call it the product introduction outlook, as you discuss with your vendors, kind of the way they're thinking about the balance of the year?

R. Michael Mohan - *Best Buy Co., Inc. - President & COO*

Yes. Scott, it's Mike. No, I don't see any change to some of the known product delivery days. There's lots of things that even we don't know. But we made a statement in the script. We think innovation is going to accelerate. There are some product categories and the ways that things come to light that I think are meaningful. I mean literally 4 months ago, most people who had a front-facing video camera on their laptop was putting a piece of tape over it. And now you need a high-resolution camera and a better set of speakers and microphone because you need to be more productive in doing videoconferencing. So I'm actually pretty excited about maybe some additional innovation or some product perhaps that we can help accelerate and commercialize and bring to market.

Operator

We will now take our next question from Jonathan Matuszewski from Jefferies.

Jonathan Richard Matuszewski - *Jefferies LLC, Research Division - Equity Analyst*

Curious if you could give us an update on your lease-to-own effort. Presumably, something that's been more challenging to facilitate with kind of limited store operations. But how do you see that evolving, especially with kind of underbanked consumers maybe feeling their wallet's pinched a bit? And any commentary on what you were able to see during the quarter.

R. Michael Mohan - *Best Buy Co., Inc. - President & COO*

Sure. Yes, absolutely. I think the ability to provide another purchasing option for customers is critically important, especially in this -- a very uncertain time for most people. The reality is in this quarter, currently, customers can only purchase through lease-to-own in our stores. And so that obviously hasn't made that program advance too much in the quarter. We are still expecting to launch it online this year, and I think that is in July. So we're still very pleased about the relationships. We're still very excited about the opportunity that it provides in extending more financing to more people and the customers that it might attract. But clearly, in the quarter, a bit of disruption just in the fact that our stores are closed to foot traffic for half of it.

Jonathan Richard Matuszewski - *Jefferies LLC, Research Division - Equity Analyst*

Yes. That's helpful. And then just a quick follow-up. Just since the pandemic started, have you seen any evidence of trade-down? Obviously, you're seeing indications of demand across categories. But any indications in terms of moving towards smaller versions of appliances or less features or last year's models or anything like that, that would indicate consumer caution?

Corie Sue Barry - *Best Buy Co., Inc. - CEO & Director*

I'll start and Mike can pile on. I don't -- we really, for the most part, have not. Now back to what Mike said about the need around your home office or the need around learning. When you're purchasing in that very kind of needs-based way, it's less about trying to trade down, it's more about trying to figure out what exactly is going to fulfill the need for you in your home. That's actually, we're seeing it in cooking and preparing food at home. We're seeing it in learning and office at home.

And so I think for us, we're actually right now seeing the demand is across the profile of what we sell. And in fact, in some spaces, it's even higher in some of the higher-end computing. I mean one of the things that's selling really well in computing is high-end computing, that's gaming computing. And gaming computing is actually some of the highest-end product that we sell. And you can definitely see that people, as they get bored in their home, are looking for some ways to entertain themselves, and have not been looking for the cheapest way to do that.

R. Michael Mohan - *Best Buy Co., Inc. - President & COO*

Yes. The one thing I would add, Jonathan, is during the time frame, a couple of the mass channel retailers were open. So from an assortment and a comparability standpoint, consumers didn't have a wholesome shopping experience. There was a couple of examples where, on constrained products, there probably was some ASP erosion based on the fact that all you had were lower-priced items. And that sometimes is very temporal, where somebody would trade down, but that's not indicative of a long-term trend in any way, shape or form. The best example is us having consultations back in place for the 700 stores and the interest level we're seeing for consumers in some of our more complex categories.

Operator

We will now take our next question from Joe Feldman from Telsey Advisory Group.

Joseph Isaac Feldman - *Telsey Advisory Group LLC - Senior MD, Assistant Director of Research & Senior Research Analyst*

I want to follow up on the CapEx reduction, I know you described a little bit on the call -- in the prepared remarks, but can you help us better understand like what are you cutting and what are you keeping? I mean, because it's -- a vast majority of it, you're still going to be spending this year, and I'm just wondering where that is relative to the cuts.

Matthew M. Bilunas - *Best Buy Co., Inc. - CFO*

Sure. I'll start and maybe Corie and Mike can jump in. I think where we've tried to cut from a CapEx perspective is mostly around discretionary, nonessential things. And actually, the fact that our stores have been closed to foot traffic for quite a while, I think there's some things that, like store remodels, don't make as much sense in the middle of what we're dealing with as they would be otherwise. So store remodels have been paused. We've lowered the amount of electronic sign labels that we were going to put in our stores simply because there's an issue of just when we can actually accomplish that in the year.

So there's more discretionary items that aren't as essential during this period that we've decided to pull back on, but there's a continuation of strategies because we still believe we're very relevant to the customer and our strategies are very applicable going forward, if not more. So there's things like automation and just dot-com technology and other things that we are just as passionate as we were before about it. And we'll continue to invest where we can to drive and accelerate our strategies.

Corie Sue Barry - *Best Buy Co., Inc. - CEO & Director*

We said it on the call, our investment in digital and supply chain automation technologies are a huge part of what allowed us to first move to curbside and then set up appointment-based scheduling. Both of those required heavy digital builds behind the scenes in order to make an app, as an example, ready for a customer to make an appointment or for an employee to be able to see who's in the queue waiting for an appointment. And we believe continued investment in those experiences, that are going to deliver choice to customers and continue to deliver with speed, are absolutely crucial to maintaining our positioning as the year goes on here.

Joseph Isaac Feldman - *Telsey Advisory Group LLC - Senior MD, Assistant Director of Research & Senior Research Analyst*

And if I could ask you one more. With regard to the 40 stores that are closed, I know you guys decided to close those and they still remain closed. Will those reopen? Or are you thinking those were kind of weaker stores that you may take advantage of this situation and keep them closed for now -- or for good, I mean.

Corie Sue Barry - *Best Buy Co., Inc. - CEO & Director*

No, they're not weaker stores. These are literally -- for the most part, it's us looking at the kind of spread of the virus and our available employee population. In a lot of cases, they're actually some of the bigger stores. On the East Coast, you can imagine, are some that we've either closed, or in a couple of situations, we still have some government mandates. So that -- don't take those 40 as they're underperforming. These are literally 40 that just it makes a lot of sense based on health, safety and government regulations.

Operator

We will now take our next question from Simeon Gutman from Morgan Stanley.

Simeon Ari Gutman - *Morgan Stanley, Research Division - Executive Director*

First, a strategic question on health care initiatives. It feels like -- or it seems like it's a pretty good moment to advance some of those strategies. Can you talk about anything with regard to user trends, level of interest in those business models, and the degree to which you can accelerate some of those -- some of that business segment?

Corie Sue Barry - *Best Buy Co., Inc. - CEO & Director*

I'm going to start by building on where Mike had left off on the consumer side of health. And I'm going to think about this writ large, everything from kind of health and fitness all the way to taking your temperature and blood pressure cuffs. There is significant demand for technology that will help us maintain and monitor our health at home, and we have seen that across the board. And this is just hypothesis, but my personal hypothesis would be, back to the point that we were talking about earlier, the level of innovation in health at home is only going to accelerate from here. Not just because people want it, but also because what you've seen is a change in reimbursement for telehealth at the overarching kind of government level. And so that combination of things is incredibly powerful on the consumer side.

Now of course, what's a little tricky there is as it relates to specifically our GreatCall devices, the phones, the wearable devices, much of those sales go through our stores. And so without our stores physically being open, it's a little harder to transact that online. So the in-the-moment pressure we're feeling is a little bit around our stores not being open. But the potential for devices that are going to keep us connected to our -- especially elderly loved ones right now, and also just keep us connected, is incredibly high.

We hit a little bit on the commercial side in the scripts. You can imagine, there's a great deal of interest around how, at a much broader scale, we can monitor people's health and take care of them in their homes. If this pandemic has highlighted anything, it is that keeping people at home as long as possible, but also tracking their vitals, tracking how they're feeling is incredibly important. So the potential on commercial, I think, has come to light even faster. This was our hypothesis, was that more people would need to have more care in their homes on the back of technology, and I think this has accelerated that hypothesis meaningfully.

Simeon Ari Gutman - *Morgan Stanley, Research Division - Executive Director*

Makes sense. And I have a follow-up on gross margin. The pressure you saw related to supply chain, the mix shift, was that normal course of mix shift? Or this was a triage situation?

And then the other question is the credit card. Is there any way you can dimensionalize impact from lower profit share? I realize you did this quarter. But the go forward, if the delinquencies grow a certain percentage, we could see a certain percentage impact to your P&L?

Matthew M. Bilunas - *Best Buy Co., Inc. - CFO*

Yes. Thank you. On the gross margin side from a channel. So obviously, in the quarter, about halfway through, we shifted filling mostly through our -- actually selling mostly through our online channel and fulfilling through our stores in a large percentage of the cases. When that happens, you incur a much higher parcel expense even though a large number of customers are still deciding to come pick up at our stores. And actually, our stores are still fulfilling a large percent of those products.

Almost 65% of what's actually happening in the quarter was either picked up at our stores curbside and/or shipped out of our stores. So with that, parcel costs just go up, and that's kind of the variable cost of online. It wasn't abnormal with that shift, it was just the normal shift to that channel when that happens. So we'd expect that to continue as we look into Q2. Obviously, half of our Q1 was under the old model and then we had -- saw the dramatic increase. We still expect online, as we said, to be significantly higher in Q2, which would mean we would incur some additional parcel cost and more gross product pressure because of it.

We have never given -- on the financing profit share, we've never given the actual number of what the profit share is. We did discuss or say that it was 20 basis points of pressure in Q1. I think we also believe it will be a pressure in Q2. I would expect it to be pretty consistent, if not maybe a little bit more in Q2 as you look forward. Hard to know how that plays out for the whole year because a big part of this has to do with the macro and unemployment. And we're -- a little too early to tell how much that actually is going to be an impact for the year, but we would expect it to be a pressure.

Corie Sue Barry - *Best Buy Co., Inc. - CEO & Director*

Thank you so much. And with that, I think that ends our call for today. Thank you all so much for joining us today, and we look forward to updating you on our progress again next quarter.

Operator

Ladies and gentlemen, this concludes today's call. Thank you for your participation. You may now disconnect.
