

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549**

**FORM 10-Q**

(Mark One)

**QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 27, 2020

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 000-49850

**BIG 5 SPORTING GOODS CORPORATION**

(Exact name of registrant as specified in its charter)

Delaware

(State or Other Jurisdiction of Incorporation or Organization)

95-4388794

(I.R.S. Employer Identification No.)

2525 East El Segundo Boulevard

El Segundo, California

(Address of Principal Executive Offices)

90245

(Zip Code)

Registrant's telephone number, including area code: (310) 536-0611

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, \$0.01 par value	BGFV	The Nasdaq Stock Market LLC

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input checked="" type="checkbox"/>	Smaller reporting company	<input checked="" type="checkbox"/>
Emerging growth company	<input type="checkbox"/>		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

There were 21,906,668 shares of common stock, with a par value of \$0.01 per share outstanding as of October 20, 2020.

**BIG 5 SPORTING GOODS CORPORATION**  
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**PART I. FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**BIG 5 SPORTING GOODS CORPORATION**  
**UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS**  
(In thousands, except share amounts)

	September 27, 2020	December 29, 2019
<b>ASSETS</b>		
Current assets:		
Cash	\$ 55,695	\$ 8,223
Accounts receivable, net of allowances of \$45 and \$58, respectively	11,018	13,646
Merchandise inventories, net	254,512	309,315
Prepaid expenses	9,192	9,680
Total current assets	<u>330,417</u>	<u>340,864</u>
Operating lease right-of-use assets, net	290,374	262,588
Property and equipment, net	60,064	68,414
Deferred income taxes	14,494	13,619
Other assets, net of accumulated amortization of \$2,310 and \$2,043, respectively	3,008	3,315
Total assets	<u>\$ 698,357</u>	<u>\$ 688,800</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 87,048	\$ 83,655
Accrued expenses	74,158	64,935
Current portion of operating lease liabilities	75,316	71,542
Current portion of finance lease liabilities	2,417	2,678
Total current liabilities	<u>238,939</u>	<u>222,810</u>
Operating lease liabilities, less current portion	230,705	206,806
Finance lease liabilities, less current portion	2,967	4,787
Long-term debt	—	66,559
Other long-term liabilities	12,513	7,466
Total liabilities	<u>485,124</u>	<u>508,428</u>
Commitments and contingencies		
Stockholders' equity:		
Common stock, \$0.01 par value, authorized 50,000,000 shares; issued 25,555,381 and 25,314,289 shares, respectively; outstanding 21,905,168 and 21,664,076 shares, respectively	255	252
Additional paid-in capital	121,262	120,054
Retained earnings	134,243	102,593
Less: Treasury stock, at cost; 3,650,213 shares	(42,527)	(42,527)
Total stockholders' equity	<u>213,233</u>	<u>180,372</u>
Total liabilities and stockholders' equity	<u>\$ 698,357</u>	<u>\$ 688,800</u>

See accompanying notes to unaudited condensed consolidated financial statements.

**BIG 5 SPORTING GOODS CORPORATION**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(In thousands, except per share data)

	13 Weeks Ended		39 Weeks Ended	
	September 27, 2020	September 29, 2019	September 27, 2020	September 29, 2019
Net sales	\$ 304,959	\$ 266,150	\$ 750,630	\$ 752,401
Cost of sales	194,924	180,158	503,847	517,416
Gross profit	110,035	85,992	246,783	234,985
Selling and administrative expense	71,337	76,886	201,040	221,676
Other income	—	—	(2,500)	—
Operating income	38,698	9,106	48,243	13,309
Interest expense	199	683	1,683	2,197
Income before taxes	38,499	8,423	46,560	11,112
Income tax expense	10,106	2,026	11,642	3,023
Net income	<u>\$ 28,393</u>	<u>\$ 6,397</u>	<u>\$ 34,918</u>	<u>\$ 8,089</u>
Earnings per share:				
Basic	<u>\$ 1.33</u>	<u>\$ 0.30</u>	<u>\$ 1.64</u>	<u>\$ 0.38</u>
Diluted	<u>\$ 1.31</u>	<u>\$ 0.30</u>	<u>\$ 1.63</u>	<u>\$ 0.38</u>
Weighted-average shares of common stock outstanding:				
Basic	<u>21,310</u>	<u>21,132</u>	<u>21,237</u>	<u>21,093</u>
Diluted	<u>21,725</u>	<u>21,154</u>	<u>21,464</u>	<u>21,125</u>

See accompanying notes to unaudited condensed consolidated financial statements.

**BIG 5 SPORTING GOODS CORPORATION**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
(In thousands, except share amounts)

	13 Weeks Ended September 27, 2020					
	Common Stock		Additional Paid-In Capital	Retained Earnings	Treasury Stock, At Cost	Total
	Shares	Amount				
Balance as of June 28, 2020	21,901,208	\$ 255	\$ 120,835	\$ 108,041	\$ (42,527)	\$ 186,604
Net income	—	—	—	28,393	—	28,393
Dividends on common stock (\$0.10 per share)	—	—	—	(2,191)	—	(2,191)
Exercise of share option awards	5,175	—	27	—	—	27
Share-based compensation	—	—	400	—	—	400
Forfeiture of nonvested share awards	(1,215)	—	—	—	—	—
Balance as of September 27, 2020	<u>21,905,168</u>	<u>\$ 255</u>	<u>\$ 121,262</u>	<u>\$ 134,243</u>	<u>\$ (42,527)</u>	<u>\$ 213,233</u>

	13 Weeks Ended September 29, 2019					
	Common Stock		Additional Paid-In Capital	Retained Earnings	Treasury Stock, At Cost	Total
	Shares	Amount				
Balance as of June 30, 2019	21,684,601	\$ 253	\$ 119,145	\$ 97,996	\$ (42,527)	\$ 174,867
Net income	—	—	—	6,397	—	6,397
Dividends on common stock (\$0.05 per share)	—	—	—	(1,077)	—	(1,077)
Share-based compensation	—	—	457	—	—	457
Forfeiture of nonvested share awards	(12,915)	—	—	—	—	—
Balance as of September 29, 2019	<u>21,671,686</u>	<u>\$ 253</u>	<u>\$ 119,602</u>	<u>\$ 103,316</u>	<u>\$ (42,527)</u>	<u>\$ 180,644</u>

	39 Weeks Ended September 27, 2020					
	Common Stock		Additional Paid-In Capital	Retained Earnings	Treasury Stock, At Cost	Total
	Shares	Amount				
Balance as of December 29, 2019	21,664,076	\$ 252	\$ 120,054	\$ 102,593	\$ (42,527)	\$ 180,372
Net income	—	—	—	34,918	—	34,918
Dividends on common stock (\$0.15 per share)	—	—	—	(3,268)	—	(3,268)
Issuance of nonvested share awards	321,600	3	(3)	—	—	—
Exercise of share option awards	5,175	—	27	—	—	27
Share-based compensation	—	—	1,281	—	—	1,281
Forfeiture of nonvested share awards	(21,110)	—	—	—	—	—
Retirement of common stock for payment of withholding tax	(64,573)	—	(97)	—	—	(97)
Balance as of September 27, 2020	<u>21,905,168</u>	<u>\$ 255</u>	<u>\$ 121,262</u>	<u>\$ 134,243</u>	<u>\$ (42,527)</u>	<u>\$ 213,233</u>

	39 Weeks Ended September 29, 2019					
	Common Stock		Additional Paid-In Capital	Retained Earnings	Treasury Stock, At Cost	Total
	Shares	Amount				
Balance as of December 30, 2018	21,424,094	\$ 250	\$ 118,351	\$ 98,787	\$ (42,527)	\$ 174,861
Cumulative adjustment from change in accounting principle, net of tax	—	—	—	(339)	—	(339)
Net income	—	—	—	8,089	—	8,089
Dividends on common stock (\$0.15 per share)	—	—	—	(3,221)	—	(3,221)
Issuance of nonvested share awards	338,256	4	(4)	—	—	—
Share-based compensation	—	—	1,475	—	—	1,475
Forfeiture of nonvested share awards	(31,570)	—	—	—	—	—
Retirement of common stock for payment of withholding tax	(59,094)	(1)	(220)	—	—	(221)
Balance as of September 29, 2019	<u>21,671,686</u>	<u>\$ 253</u>	<u>\$ 119,602</u>	<u>\$ 103,316</u>	<u>\$ (42,527)</u>	<u>\$ 180,644</u>

See accompanying notes to unaudited condensed consolidated financial statements.

**BIG 5 SPORTING GOODS CORPORATION**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In thousands)

	39 Weeks Ended	
	September 27, 2020	September 29, 2019
<b>Cash flows from operating activities:</b>		
Net income	\$ 34,918	\$ 8,089
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	13,633	14,630
Share-based compensation	1,281	1,475
Amortization of other assets	267	195
ROU asset gain on disposal	—	(110)
Noncash lease expense	47,095	45,439
Gain on eminent domain condemnation	(2,500)	—
Proceeds from eminent domain condemnation - lost profit margin	2,263	—
Deferred income taxes	(875)	735
Changes in operating assets and liabilities:		
Accounts receivable, net	2,668	4,152
Merchandise inventories, net	54,803	(15,614)
Prepaid expenses and other assets	634	118
Accounts payable	15,302	8,969
Operating lease liabilities	(47,248)	(46,721)
Accrued expenses and other long-term liabilities	14,147	(7,705)
Net cash provided by operating activities	<u>136,388</u>	<u>13,652</u>
<b>Cash flows from investing activities:</b>		
Purchases of property and equipment	(5,041)	(6,128)
Proceeds from eminent domain condemnation - property and equipment	237	—
Net cash used in investing activities	<u>(4,804)</u>	<u>(6,128)</u>
<b>Cash flows from financing activities:</b>		
Borrowings under revolving credit facility	137,296	135,950
Payments under revolving credit facility	(203,855)	(140,308)
Changes in book overdraft	(11,973)	548
Debt issuance costs paid	(106)	—
Principal payments under finance lease liabilities	(2,067)	(1,874)
Proceeds from exercise of share option awards	27	—
Tax withholding payments for share-based compensation	(97)	(221)
Dividends paid	(3,337)	(3,342)
Net cash used in financing activities	<u>(84,112)</u>	<u>(9,247)</u>
Net increase (decrease) in cash	47,472	(1,723)
Cash at beginning of period	8,223	6,765
Cash at end of period	<u>\$ 55,695</u>	<u>\$ 5,042</u>
<b>Supplemental disclosures of non-cash investing and financing activities:</b>		
Property and equipment acquired under finance leases	\$ —	\$ 2,093
Property and equipment additions unpaid	\$ 976	\$ 1,583
<b>Supplemental disclosures of cash flow information:</b>		
Interest paid	\$ 1,714	\$ 2,150
Income taxes paid	\$ 4,213	\$ 725

See accompanying notes to unaudited condensed consolidated financial statements.

**BIG 5 SPORTING GOODS CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(1) Description of Business**

Big 5 Sporting Goods Corporation (the “Company”) is a leading sporting goods retailer in the western United States, operating 431 stores and an e-commerce platform as of September 27, 2020. The Company provides a full-line product offering in a traditional sporting goods store format that averages approximately 11,000 square feet. The Company’s product mix includes athletic shoes, apparel and accessories, as well as a broad selection of outdoor and athletic equipment for team sports, fitness, camping, hunting, fishing, tennis, golf, winter and summer recreation and roller sports. The Company is a holding company that operates as one reportable segment through Big 5 Corp., its 100%-owned subsidiary, and Big 5 Services Corp., which is a 100%-owned subsidiary of Big 5 Corp. Big 5 Services Corp. provides a centralized operation for the issuance and administration of gift cards and returned merchandise credits (collectively, “stored-value cards”).

The accompanying interim unaudited condensed consolidated financial statements (“Interim Financial Statements”) of the Company and its 100%-owned subsidiaries have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information and are presented in accordance with the requirements of Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, these Interim Financial Statements do not include all of the information and notes required by GAAP for complete financial statements. These Interim Financial Statements should be read in conjunction with the consolidated financial statements and notes thereto for the fiscal year ended December 29, 2019 included in the Company’s Annual Report on Form 10-K. In the opinion of management, the Interim Financial Statements included herein contain all adjustments, including normal recurring adjustments, considered necessary to present fairly the Company’s financial position, the results of operations and cash flows for the periods presented.

The operating results and cash flows of the interim periods presented herein are not necessarily indicative of the results to be expected for any other interim period or the full year.

**(2) Summary of Significant Accounting Policies**

*Consolidation*

The accompanying Interim Financial Statements include the accounts of Big 5 Sporting Goods Corporation, Big 5 Corp. and Big 5 Services Corp. Intercompany balances and transactions have been eliminated in consolidation.

*Reporting Period*

The Company follows the concept of a 52-53 week fiscal year, which ends on the Sunday nearest December 31. Fiscal year 2020 is comprised of 53 weeks and ends on January 3, 2021. Fiscal year 2019 was comprised of 52 weeks and ended on December 29, 2019. The first three quarters in fiscal 2020 are each comprised of 13 weeks, and the fourth quarter of fiscal 2020 is comprised of 14 weeks. The four quarters of fiscal 2019 were each comprised of 13 weeks.

*Recently Adopted Accounting Updates*

In August 2018, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2018-13, *Fair Value Measurements (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement*. This standard removes, modifies, and adds certain disclosure requirements for fair value measurements, and is effective for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2019, with early adoption permitted. The Company adopted ASU No. 2018-13 in the first quarter of fiscal 2020, coinciding with the standard’s effective date, and the impact from this standard was immaterial.

**BIG 5 SPORTING GOODS CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(continued)**

In August 2018, the FASB issued ASU No. 2018-15, *Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract*. This standard aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). The Company’s accounting for the service element of a hosting arrangement that is a service contract is not affected by the proposed amendments and will continue to be expensed as incurred in accordance with existing guidance. This standard does not expand on existing disclosure requirements except to require a description of the nature of hosting arrangements that are service contracts. This standard is effective for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2019, and can be adopted either prospectively or retrospectively. Accordingly, the Company adopted the updated disclosure requirements of ASU No. 2018-15 prospectively in the first quarter of fiscal 2020, coinciding with the standard’s effective date, and the impact from this standard was immaterial.

In December 2019, the FASB issued ASU No. 2019-12, *Simplifying the Accounting for Income Taxes*. This standard simplifies the accounting for income taxes by removing certain exceptions to the general principles in ASC 740, *Income Taxes*, while also clarifying and amending existing guidance, including interim-period accounting for enacted changes in tax law. This standard is effective for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2020, with early adoption permitted. The Company adopted ASU No. 2019-12 in the first quarter of fiscal 2020 and the impact from this standard was immaterial.

*Recently Issued Accounting Updates*

In March 2020, the FASB issued ASU No. 2020-04, *Reference Rate Reform (Topic 848)—Facilitation of the Effects of Reference Rate Reform on Financial Reporting*. This standard provides optional guidance for a limited time to ease the potential burden in accounting for (or recognizing the effects of) reference rate reform on financial reporting. The amendments in this standard apply only to contracts and hedging relationships that reference LIBOR or another reference rate expected to be discontinued due to reference rate reform. The expedients and exceptions provided by the amendments do not apply to contract modifications made and hedging relationships entered into or evaluated after December 31, 2022. The amendments in this standard are elective and are effective upon issuance for all entities. The Company is evaluating the expedients and exceptions provided by the amendments in this standard to determine their impact.

Other recently issued accounting updates are not expected to have a material impact on the Company’s Interim Financial Statements.

*COVID-19 Impact on Concentration of Risk*

The novel coronavirus (“COVID-19”) pandemic has significantly impacted health and economic conditions throughout the United States and globally, as public concern about becoming ill with the virus has led to the issuance of recommendations and/or mandates from federal, state and local authorities to practice social distancing or self-quarantine.

The Company primarily operates traditional sporting goods retail stores located in the western United States, with approximately 52% of its stores, along with its corporate offices and distribution center, located in California. Because of this, the Company is subject to regional risks, including the impact of the COVID-19 outbreak. Beginning on March 20, 2020, the Company temporarily closed more than one-half of its retail store locations in response to state and local shelter orders related to the COVID-19 outbreak. The Company was subsequently able to gradually reopen its store locations based on initially qualifying as an “essential” business under applicable regulations and later as a result of the easing of regulatory restrictions on retail operations in the Company’s market areas. As of the end of the second quarter of fiscal 2020, all of the Company’s stores that were temporarily closed due to COVID-19 had reopened for in-store shopping, subject to appropriate social distancing restrictions and with reduced operating hours. These restrictions and reduced operating hours continued into the third quarter of fiscal 2020. New temporary closures of stores may be required if additional orders are issued in response to changing health conditions. Additionally, during the second and third fiscal quarters, the pandemic and the shelter orders that were in place in the Company’s market areas negatively impacted customer traffic into the Company’s stores. In an effort to promote social distancing protocols, the Company has implemented reduced store hours, limited the number of customers in its stores at any one time and has generally implemented social-distancing guidelines throughout the store operating space. Due to the reduced customer traffic, and in an effort to preserve capital, the Company implemented temporary and permanent workforce reductions throughout the organization, and reduced advertising and planned capital spending in fiscal 2020. The Company also temporarily reduced merchandise inventory orders, which could impact product availability in the Company’s stores and sales in future periods. The Company may further restrict its store operations and operations in its distribution facility if deemed necessary or if recommended or mandated by authorities.

**BIG 5 SPORTING GOODS CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(continued)**

A substantial amount of the Company's inventory is manufactured abroad. COVID-19 has also impacted the Company's supply chain for products sold, particularly those products that are sourced from China. To the extent one or more vendors is negatively impacted by COVID-19, including due to the closure of those vendors' distribution centers or manufacturing facilities, the Company may be unable to maintain delivery schedules or adequate inventory in its stores.

*Use of Estimates*

Management makes a number of estimates and assumptions relating to the reporting of assets, liabilities and stockholders' equity and the disclosure of contingent assets and liabilities at the date of the Interim Financial Statements and reported amounts of revenue and expense during the reporting period to prepare these Interim Financial Statements in conformity with GAAP. Certain items subject to such estimates and assumptions include the carrying amount of merchandise inventories, property and equipment, lease assets and lease liabilities; valuation allowances for receivables, sales returns and deferred income tax assets; estimates related to stored-value cards and the valuation of share-based compensation awards; and obligations related to litigation, self-insurance liabilities and employee benefits. Due to the inherent uncertainty involved in making assumptions and estimates, events and changes in circumstances arising after September 27, 2020, including those resulting from the impacts of the COVID-19 pandemic, may result in actual outcomes that differ from those contemplated by management's assumptions and estimates.

*Revenue Recognition*

The Company operates solely as a sporting goods retailer, which includes both retail stores and an e-commerce platform, that offers a broad range of products in the western United States and online. Generally, all revenue is recognized when control of the promised goods is transferred to customers, for an amount that reflects the consideration in exchange for those goods. Accordingly, the Company implicitly enters into a contract with customers to deliver merchandise inventory at the point of sale. Collectability is reasonably assured since the Company only extends immaterial credit purchases to certain municipalities and local school districts.

In accordance with ASC 606, *Revenue from Contracts with Customers*, the Company disaggregates net sales into the following major merchandise categories to depict the nature and amount of revenue and related cash flows:

	13 Weeks Ended		39 Weeks Ended	
	September 27, 2020	September 29, 2019	September 27, 2020	September 29, 2019
	(In thousands)			
Hardgoods	\$ 201,993	\$ 145,974	\$ 461,040	\$ 383,193
Athletic and sport footwear	59,654	73,277	164,685	208,902
Athletic and sport apparel	41,712	45,466	120,721	155,931
Other sales	1,600	1,433	4,184	4,375
Net sales	<u>\$ 304,959</u>	<u>\$ 266,150</u>	<u>\$ 750,630</u>	<u>\$ 752,401</u>

Substantially all of the Company's revenue is for single performance obligations for the following distinct items:

- Retail store sales
- E-commerce sales
- Stored-value cards

For performance obligations related to retail store and e-commerce sales contracts, the Company typically transfers control, for retail stores, upon consummation of the sale when the product is paid for and taken by the customer and, for e-commerce sales, when the product is tendered for delivery to the common carrier. For performance obligations related to stored-value cards, the Company typically transfers control upon redemption of the stored-value card through consummation of a future sales transaction. The Company accounts for shipping and handling relative to e-commerce sales as fulfillment activities, and not a separate performance obligation. Accordingly, the Company recognizes revenue for only one performance obligation, the sale of the product, at shipping point (when the customer gains control). Revenue associated with e-commerce sales was not material for the 13 and 39 weeks ended September 27, 2020 and September 29, 2019.

**BIG 5 SPORTING GOODS CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(continued)**

The Company recognized \$1.3 million and \$3.9 million in stored-value card redemption revenue for the 13 and 39 weeks ended September 27, 2020, respectively, compared to \$1.5 million and \$5.2 million in stored-value card redemption revenue for the 13 and 39 weeks ended September 29, 2019, respectively. The Company also recognized \$0.1 million and \$0.2 million in stored-value card breakage revenue for the 13 and 39 weeks ended September 27, 2020, respectively, compared to \$0.1 million and \$0.3 million for the 13 and 39 weeks ended September 29, 2019, respectively. The Company had outstanding stored-value card liabilities of \$6.4 million and \$7.2 million as of September 27, 2020 and December 29, 2019, respectively, which are included in accrued expenses in the accompanying interim unaudited condensed consolidated balance sheets. Based upon historical experience, stored-value cards are predominantly redeemed in the first two years following their issuance date.

The Company recorded, as prepaid expense, estimated right-of-return merchandise cost of \$0.8 million and \$1.4 million related to estimated sales returns as of September 27, 2020 and December 29, 2019, respectively, and recorded, in accrued expenses in the accompanying interim unaudited condensed consolidated balance sheets, an allowance for sales returns reserve of \$1.6 million and \$2.7 million as of September 27, 2020 and December 29, 2019, respectively.

*Share-Based Compensation*

The Company accounts for its share-based compensation in accordance with ASC 718, *Compensation—Stock Compensation*. The Company recognizes compensation expense on a straight-line basis over the requisite service period using the fair-value method for share option awards, nonvested share awards and nonvested share unit awards granted with service-only conditions. See Note 10 to the Interim Financial Statements for a further discussion on share-based compensation.

*Valuation of Merchandise Inventories, Net*

The Company's merchandise inventories are made up of finished goods and are valued at the lower of cost or net realizable value using the weighted-average cost method that approximates the first-in, first-out ("FIFO") method. Average cost includes the direct purchase price of merchandise inventory, net of vendor allowances and cash discounts, in-bound freight-related expense and allocated overhead expense associated with the Company's distribution center.

Management regularly reviews inventories and records valuation reserves for damaged and defective merchandise, merchandise items with slow-moving or obsolescence exposure and merchandise that has a carrying value that exceeds net realizable value. Because of its merchandise mix, the Company has not historically experienced significant occurrences of obsolescence.

Inventory shrinkage is accrued as a percentage of merchandise sales based on historical inventory shrinkage trends. The Company performs physical inventories of its stores at least once per year and cycle counts inventories at its distribution center throughout the year. The reserve for inventory shrinkage primarily represents an estimate for inventory shrinkage for each store since the last physical inventory date through the reporting date.

These reserves are estimates, which could vary significantly, either favorably or unfavorably, from actual results if future economic conditions, consumer demand and competitive environments differ from expectations.

*Valuation of Long-Lived Assets*

In accordance with ASC 360, *Property, Plant, and Equipment*, the Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

Long-lived assets are reviewed for recoverability at the lowest level in which there are identifiable cash flows ("asset group"), usually at the store level. The carrying amount of a store asset group includes stores' property and equipment, leasehold improvements and operating lease right-of-use ("ROU") assets. The carrying amount of a store asset group is not considered recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the store asset group. When stores are identified as having an indicator of impairment, the Company forecasts undiscounted cash flows over the store asset group's remaining lease term and compares the undiscounted cash flows to the carrying amount of the store asset group. If the store asset group is determined not to be recoverable, then an impairment charge will be recognized in the amount by which the carrying amount of the store asset group exceeds its fair value, determined using discounted cash flow valuation techniques, as contemplated in ASC 820, *Fair Value Measurements*.

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The Company determines the cash flows expected to result from the store asset group by projecting future revenue, gross margin and operating expense for each store asset group under evaluation for impairment. The estimates of future cash flows involve management judgment and are based upon assumptions about expected future operating performance. Assumptions used in these forecasts are consistent with internal planning, and include assumptions about sales growth rates, gross margins and operating expense in relation to the current economic environment and the Company's future expectations, competitive factors in its various markets, inflation, sales trends and other relevant environmental factors that may impact the store under evaluation. The actual cash flows could differ from management's estimates due to changes in business conditions, operating performance and economic conditions. If economic conditions deteriorate in the markets in which the Company conducts business, or if other negative market conditions develop, the Company may experience additional impairment charges in the future for underperforming stores.

The resulting impairment charge, if any, is allocated to the property and equipment, leasehold improvements and operating lease ROU assets on a pro rata basis using the relative carrying amounts of those assets. The allocated impairment charge to a long-lived asset is limited to the extent that the impairment charge does not reduce the carrying amount of the long-lived asset below its individual fair value. The estimation of the fair value of an ROU asset involves the evaluation of current market value rental amounts for leases associated with ROU assets. The estimates of current market value rental amounts are primarily based on recent observable market rental data of other comparable retail store locations. The fair value of an ROU asset is measured using a discounted cash flow valuation technique by discounting the estimated current and future market rental values using a property-specific discount rate.

The Company did not recognize any impairment charges in the first nine months of fiscal 2020 or 2019.

*Leases*

In accordance with ASC 842, *Leases*, the Company determines if an arrangement is a lease at inception. The Company has operating and finance leases for the Company's retail store facilities, distribution center, corporate offices, information technology hardware, and distribution center delivery tractors and equipment. Operating leases are included in operating lease ROU assets and operating lease liabilities, current and noncurrent, on the interim unaudited condensed consolidated balance sheet. Finance leases are included in property and equipment and finance lease liabilities on the interim unaudited condensed consolidated balance sheets. Lease liabilities are calculated using the effective interest method, regardless of classification, while the amortization of ROU assets varies depending upon classification. Finance lease classification results in a front-loaded expense recognition pattern over the lease term which amortizes the ROU asset by recognizing interest expense and amortization expense as separate components of lease expense and calculates the amortization expense component on a straight-line basis. Conversely, operating lease classification results in a straight-line expense recognition pattern over the lease term and recognizes lease expense as a single expense component, which results in amortization of the ROU asset that equals the difference between lease expense and interest expense. Lease expense for finance and operating leases are included in cost of sales or selling and administrative expense, based on the use of the leased asset, on the interim unaudited condensed consolidated statement of operations. Variable payments such as property taxes, insurance and common area maintenance related to triple net leases, as well as certain equipment sales taxes, licenses, fees and repairs, are expensed as incurred, and leases with an initial term of 12 months or less are excluded from minimum lease payments and are not recorded on the balance sheet. The Company recognizes variable lease expense for these short-term leases on a straight-line basis over the remaining lease term.

ROU assets represent the right to use an underlying asset for the lease term and lease liabilities represent the obligation to make lease payments arising from the lease. Operating lease ROU assets and liabilities are recognized at the commencement date based on the present value of lease payments over the reasonably certain lease term. As the Company's leases generally do not provide an implicit rate, the Company uses a collateralized incremental borrowing rate ("IBR") to determine the present value of lease payments. The collateralized IBR is based on a synthetic credit rating that is externally prepared on an annual basis. This analysis considers qualitative and quantitative factors based on guidance provided by a rating agency for the consumer durables industry. The Company adjusts the selected IBR quarterly with a company-specific unsecured yield curve that approximates the Company's market risk profile. The collateralized IBR is also based upon the estimated impact that the collateral has on the IBR. To account for the collateralized nature of the IBR, the Company utilized a notching method based on notching guidance provided by a rating agency whereby the Company's base credit rating is notched upward as the yield curve on a secured loan is expected to be lower versus an unsecured loan.

The operating lease ROU asset also includes any prepaid lease payments made and is reduced by lease incentives such as tenant improvement allowances. The operating lease terms may include options to extend or terminate the lease when it is reasonably certain that the Company will exercise that option. Operating lease expense for lease payments is recognized on a straight-line basis over the lease term.

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Certain of the leases for the Company's retail store facilities provide for payments based on future sales volumes at the leased location, which are not measurable at the inception of the lease. Under ASC 842, these contingent rents are expensed as they accrue.

In response to the large volume of anticipated lease concessions to be granted related to the effects of the COVID-19 pandemic, and the resultant expected cost and complexity of applying the lease modification requirements in ASC 842, the FASB issued Staff Q&A—Topic 842 and Topic 840: *Accounting For Lease Concessions Related to the Effects of the COVID-19 Pandemic*, in April 2020 as interpretive guidance to provide clarity in response to the crisis. The FASB staff indicated that it would be acceptable for entities to make an election to account for lease concessions related to the effects of the COVID-19 pandemic consistent with how they would be accounted for as though enforceable rights and obligations for those concessions existed in the original contract. Consequently, for such lease concessions, an entity will not need to reassess each existing contract to determine whether enforceable rights and obligations for concessions exist and an entity can elect to apply or not to apply the lease modification guidance in ASC 842 to those contracts. The election is available for concessions related to the effects of the COVID-19 pandemic that result in the total payments required by the modified contract being substantially the same as or less than total payments required by the original contract.

In accordance with this interpretive guidance, the Company elected to account for lease concessions related to the effects of the COVID-19 pandemic that resulted in the total payments required by the modified contract being substantially the same as or less than total payments required by the original contract consistent with how they would be accounted for as though enforceable rights and obligations for those concessions existed in the original contract. Consequently, for such lease concessions, the Company did not reassess each existing contract to determine whether enforceable rights and obligations for concessions existed and elected not to apply the lease modification guidance in ASC 842 to those contracts. The Company accounted for COVID-19 lease abatements of \$3.1 million in the 39 weeks ended September 27, 2020 as reductions to variable lease expense and accounted for lease deferrals of \$0.8 million as of September 27, 2020 as if no changes to the lease contract were made while continuing to recognize expense during the deferral period and deferring the payment obligation as a liability.

See Note 5 to the Interim Financial Statements for a further discussion on leases.

**(3) Fair Value Measurements**

The carrying values of cash, accounts receivable, accounts payable and accrued expenses approximate the fair values of these instruments due to their short-term nature. The carrying amount for borrowings under the revolving credit facility (the "Credit Facility") approximates fair value because of the variable market interest rate charged to the Company for these borrowings. When the Company recognizes impairment on certain of its underperforming stores, the carrying values of these stores are reduced to their estimated fair values.

As of September 27, 2020 and December 29, 2019, the Company's only significant assets or liabilities measured at fair value on a nonrecurring basis subsequent to their initial recognition were assets subject to long-lived asset impairment related to certain underperforming stores. The Company estimated the fair values of these long-lived assets based on the Company's own judgments about the assumptions that market participants would use in pricing the asset and on observable market data of underperforming stores' specific comparable markets, when available. The Company classified these fair value measurements as Level 3 inputs, which are unobservable inputs for which market data are not available and that are developed using the best information available about pricing assumptions used by market participants in accordance with ASC 820.

**(4) Accrued Expenses**

The major components of accrued expenses are as follows:

	September 27, 2020	December 29, 2019
	(In thousands)	
Payroll and related expense	\$ 25,633	\$ 23,433
Occupancy expense	11,422	9,503
Income taxes payable	10,313	—
Sales tax	8,210	9,607
Other	18,580	22,392
Accrued expenses	<u>\$ 74,158</u>	<u>\$ 64,935</u>

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**(5) Lease Commitments**

The Company adopted ASC 842 as of December 31, 2018, using the modified retrospective approach and applying transitional relief allowing entities to initially apply the requirements at the adoption date by recognizing a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. Consequently, results and disclosures for the reporting periods beginning on December 31, 2018 are reported and presented under ASC 842. Adoption of the standard resulted in the initial recognition of operating lease ROU assets of \$262.9 million and operating lease liabilities of \$279.7 million as of December 31, 2018. The adoption of this standard did not have a material impact on the Company's interim unaudited condensed consolidated statements of operations, shareholders' equity or cash flows, and had no material impact on beginning retained earnings in fiscal 2019. Additionally, the Company elected the transition package of practical expedients permitted within the new standard which, among other things, allowed it to carry forward the historical lease classification. The Company did not elect the practical expedient to use hindsight in determining the lease term and in assessing impairment of ROU assets.

The Company has operating and finance leases for the Company's retail store facilities, distribution center, corporate offices, information technology hardware and distribution center delivery tractors and equipment, and accounts for these leases in accordance with ASC 842.

Certain of the leases for the Company's retail store facilities provide for variable payments for property taxes, insurance, common area maintenance payments related to triple net leases, as well as certain equipment sales taxes, licenses, fees, repairs, and rental payments based on future sales volumes at the leased location, which are not measurable at the inception of the lease, or rental payments that are adjusted periodically for inflation. The Company recognizes variable lease expense for these leases in the period incurred which, for contingent rent, begins in the period in which it becomes probable that the specified target that triggers the variable lease payments will be achieved. The Company's lease agreements do not contain any material residual value guarantees or material restrictive covenants.

In accordance with ASC 842, the components of lease expense were as follows:

	13 Weeks Ended		39 Weeks Ended	
	September 27, 2020	September 29, 2019	September 27, 2020	September 29, 2019
	(In thousands)			
Lease expense:				
Amortization of right-of-use assets	\$ 660	\$ 618	\$ 2,070	\$ 2,002
Interest on lease liabilities	67	91	234	286
Finance lease expense	727	709	2,304	2,288
Operating lease expense	20,382	20,254	60,986	60,079
Variable lease expense (1)	4,595	4,547	10,577	13,769
Sublease income	(293)	(373)	(879)	(1,018)
Total lease expense	<u>\$ 25,411</u>	<u>\$ 25,137</u>	<u>\$ 72,988</u>	<u>\$ 75,118</u>

- (1) Variable lease expense for the 13 and 39 weeks ended September 27, 2020 was reduced by \$0.1 million and \$3.1 million, respectively, for lease abatements related to the effects of the COVID-19 pandemic that resulted in the total payments required by the modified contract being substantially the same as or less than total payments required by the original contract. See Note 2 to the Interim Financial Statements for a further discussion on lease concessions.

Additionally, subsequent to the issuance of the Company's Interim Financial Statements as of September 29, 2019, management identified an immaterial correction related to the disclosure of certain variable lease payments. Variable lease expense for the 13 and 39 weeks ended September 29, 2019 did not previously include \$4.5 million and \$13.6 million, respectively, of variable lease payments for property taxes, insurance, and common area maintenance related to triple net leases, as well as certain equipment sales taxes, licenses, fees and repairs. Management corrected the disclosure related to variable lease expense in the table above for the 13 and 39 weeks ended September 29, 2019 and, except for this change in disclosure, the correction had no impact upon the Company's Interim Financial Statements.

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In accordance with ASC 842, other information related to leases was as follows:

	39 Weeks Ended	
	September 27, 2020	September 29, 2019
	(In thousands)	
Operating cash flows from operating leases	\$ 57,243	\$ 61,569
Operating cash flows from finance leases	234	286
Financing cash flows from finance leases	2,067	1,874
Cash paid for amounts included in the measurement of lease liabilities	\$ 59,544	\$ 63,729
Right-of-use assets obtained in exchange for new finance lease liabilities	\$ —	\$ 2,129
Right-of-use assets obtained in exchange for new operating lease liabilities	\$ 75,025	\$ 52,913
Weighted-average remaining lease term—finance leases	2.6 years	3.2 years
Weighted-average remaining lease term—operating leases	5.2 years	5.3 years
Weighted-average discount rate—finance leases	4.7%	4.8%
Weighted-average discount rate—operating leases	6.2%	6.4%

In accordance with ASC 842, maturities of finance and operating lease liabilities as of September 27, 2020 were as follows:

Year Ending:	Finance Leases	Operating Leases
	(In thousands)	
2020 (remaining three months)	\$ 874	\$ 26,842
2021	2,188	81,932
2022	1,740	72,711
2023	920	56,991
2024	—	48,381
Thereafter	—	71,245
Undiscounted cash flows	\$ 5,722	\$ 358,102
Reconciliation of lease liabilities:		
Weighted-average remaining lease term	2.6 years	5.2 years
Weighted-average discount rate	4.7%	6.2%
Present values	\$ 5,384	\$ 306,021
Lease liabilities - current	2,417	75,316
Lease liabilities - long-term	2,967	230,705
Lease liabilities - total	\$ 5,384	\$ 306,021
Difference between undiscounted and discounted cash flows	\$ 338	\$ 52,081

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**(6) Long-Term Debt**

On October 18, 2010, the Company, Big 5 Corp. and Big 5 Services Corp. entered into a credit agreement with Wells Fargo Bank, National Association (“Wells Fargo”), as administrative agent, and a syndicate of other lenders, which was amended on October 31, 2011, December 19, 2013 and September 29, 2017 (as so amended, the “Credit Agreement”), and has a maturity date of September 29, 2022.

The Credit Agreement provides for a Credit Facility with an aggregate committed availability of up to \$140.0 million, which amount may be increased (“accordion feature”) at the Company’s option up to a maximum of \$165.0 million. On March 30, 2020 the Company exercised the accordion feature of the Credit Agreement and increased the aggregate committed availability under the Credit Facility to \$165.0 million to support its liquidity initiatives during the COVID-19 pandemic. The Company may also request additional increases in aggregate availability, up to a maximum of \$200.0 million, in which case the existing lenders under the Credit Agreement will have the option to increase their commitments to accommodate the requested increase. If such existing lenders do not exercise that option, the Company may (with the consent of Wells Fargo, not to be unreasonably withheld) seek other lenders willing to provide such commitments. The Credit Agreement includes a provision which permits the Company to elect to reduce the aggregate committed availability under the Credit Agreement to \$100.0 million for a three-month period each calendar year. The Credit Facility includes a \$25.0 million sublimit for issuances of letters of credit and a \$20.0 million sublimit for swingline loans.

The Company may borrow under the Credit Facility from time to time, provided the amounts outstanding will not exceed the lesser of the then aggregate availability (as discussed above) and the Borrowing Base (such lesser amount being referred to as the “Loan Cap”). The “Borrowing Base” generally is comprised of the sum, at the time of calculation, of (a) 90.00% of eligible credit card receivables; plus (b) the cost of eligible inventory (other than eligible in-transit inventory), net of inventory reserves, multiplied by 90.00% of the appraised net orderly liquidation value of eligible inventory (expressed as a percentage of the cost of eligible inventory); plus (c) the lesser of (i) the cost of eligible in-transit inventory, net of inventory reserves, multiplied by 90.00% of the appraised net orderly liquidation value of eligible in-transit inventory (expressed as a percentage of the cost of eligible in-transit inventory), or (ii) \$10.0 million, minus (d) certain reserves established by Wells Fargo in its role as the Administrative Agent in its reasonable discretion.

Generally, the Company may designate specific borrowings under the Credit Facility as either base rate loans or LIBO rate loans. The applicable interest rate on the Company’s borrowings is a function of the daily average, over the preceding fiscal quarter, of the excess of the Loan Cap over amounts borrowed (such amount being referred to as the “Average Daily Availability”). Those loans designated as LIBO rate loans bear interest at a rate equal to the applicable adjusted LIBO rate plus an applicable margin as shown in the table below. Those loans designated as base rate loans bear interest at a rate equal to the applicable margin for base rate loans (as shown below) plus the highest of (a) the Federal funds rate, as in effect from time to time, plus one-half of one percent (0.50%), (b) the LIBO rate, plus one percentage point (1.00%), or (c) the rate of interest in effect for such day as announced from time to time within Wells Fargo as its “prime rate.” The applicable margin for all loans is a function of Average Daily Availability for the preceding fiscal quarter as set forth below.

Level	Average Daily Availability	LIBO Rate Applicable Margin	Base Rate Applicable Margin
I	Greater than or equal to \$70,000,000	1.25%	0.25%
II	Less than \$70,000,000	1.375%	0.50%

The commitment fee assessed on the unused portion of the Credit Facility is 0.20% per annum.

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Obligations under the Credit Facility are secured by a general lien and perfected security interest in substantially all of the Company's assets. The Credit Agreement contains covenants that require the Company to maintain a fixed charge coverage ratio of not less than 1.0:1.0 in certain circumstances, and limit the ability to, among other things, incur liens, incur additional indebtedness, transfer or dispose of assets, change the nature of the business, guarantee obligations, pay dividends or make other distributions or repurchase stock, and make advances, loans or investments. The Company may declare or pay cash dividends or repurchase stock only if, among other things, no default or event of default then exists or would arise from such dividend or repurchase of stock and, after giving effect to such dividend or repurchase, certain availability and/or fixed charge coverage ratio requirements are satisfied. The Credit Agreement contains customary events of default, including, without limitation, failure to pay when due principal amounts with respect to the Credit Facility, failure to pay any interest or other amounts under the Credit Facility for five days after becoming due, failure to comply with certain agreements or covenants contained in the Credit Agreement, failure to satisfy certain judgments against the Company, failure to pay when due (or any other default which does or may lead to the acceleration of) certain other material indebtedness in principal amount in excess of \$5.0 million, and certain insolvency and bankruptcy events.

As of September 27, 2020, the Company had fully paid down its long-term revolving credit borrowings to zero and had letter of credit commitments of \$4.7 million outstanding, compared with borrowings of \$66.6 million and letter of credit commitments of \$0.7 million as of December 29, 2019. Total remaining borrowing availability, after subtracting letters of credit, was \$160.3 million and \$72.7 million as of September 27, 2020 and December 29, 2019, respectively.

**(7) Income Taxes**

Under the asset and liability method prescribed under ASC 740, *Income Taxes*, the Company recognizes deferred tax assets and liabilities for the future tax consequences attributable to differences between financial statement carrying amounts of assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be realized or settled. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date. The realizability of deferred tax assets is assessed throughout the year and a valuation allowance is recorded, if necessary, to reduce net deferred tax assets to the amount more likely than not to be realized. As of September 27, 2020 and December 29, 2019, the Company had a valuation allowance for deferred income tax assets of \$1.2 million related to unused California Enterprise Zone Tax Credits, which the Company will no longer be able to carry forward beyond 2024 as a result of California's termination of this program.

The Company files a consolidated federal income tax return and files tax returns in various state and local jurisdictions. The statutes of limitations for consolidated federal income tax returns are open for fiscal years 2016 and after, and state and local income tax returns are open for fiscal years 2015 and after.

The provision for income taxes for the 39 weeks ended September 27, 2020 and September 29, 2019 reflects the write-off of deferred tax assets of \$0.3 million and \$0.4 million, respectively, related to share-based compensation.

On March 27, 2020, the Federal government enacted the U.S. Coronavirus Aid, Relief and Economic Security ("CARES") Act to provide relief from the impact of COVID-19. Among other relief, the CARES Act allows companies with a net operating loss ("NOL") in either 2018, 2019 or 2020 to carry back those losses five years. As a result, the Company amended its 2018 income tax return to carry back its 2018 NOL to a period with a higher statutory tax rate in effect at that time, and received a related income tax refund of \$2.1 million in the second quarter of fiscal 2020.

As of September 27, 2020 and December 29, 2019, the Company had no unrecognized tax benefits including those that, if recognized, would affect the Company's effective income tax rate over the next 12 months. The Company's policy is to recognize interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expense. As of September 27, 2020 and December 29, 2019, the Company had no accrued interest or penalties.

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**(8) Earnings Per Share**

The Company calculates earnings per share in accordance with ASC 260, *Earnings Per Share*, which requires a dual presentation of basic and diluted earnings per share. Basic earnings per share is calculated by dividing net income by the weighted-average shares of common stock outstanding, reduced by shares repurchased and held in treasury, during the period. Diluted earnings per share represents basic earnings per share adjusted to include the potentially dilutive effect of outstanding share option awards, nonvested share awards and nonvested share unit awards. During periods of net loss, diluted loss per share is equal to basic loss per share because the antidilutive effect of potential common shares is disregarded.

The following table sets forth the computation of basic and diluted earnings per common share:

	13 Weeks Ended		39 Weeks Ended	
	September 27, 2020	September 29, 2019	September 27, 2020	September 29, 2019
	(In thousands, except per share data)			
Net income	\$ 28,393	\$ 6,397	\$ 34,918	\$ 8,089
Weighted-average shares of common stock outstanding:				
Basic	21,310	21,132	21,237	21,093
Dilutive effect of common stock equivalents arising from share option, nonvested share and nonvested share unit awards	415	22	227	32
Diluted	21,725	21,154	21,464	21,125
Basic earnings per share	\$ 1.33	\$ 0.30	\$ 1.64	\$ 0.38
Diluted earnings per share	\$ 1.31	\$ 0.30	\$ 1.63	\$ 0.38
Antidilutive share option awards excluded from diluted calculation	268	520	700	493
Antidilutive nonvested share and nonvested share unit awards excluded from diluted calculation	120	471	144	456

The computation of diluted earnings per share for all periods presented excludes certain potential share option awards since the exercise prices of these share option awards exceeded the average market price of the Company's common shares, and the effect of their inclusion would have been antidilutive (i.e., including such share option awards would result in higher earnings per share). Additionally, the computation of diluted earnings per share for all periods presented excludes certain nonvested share awards and nonvested share unit awards that were outstanding and antidilutive, since the grant date fair values of these nonvested share awards and nonvested share unit awards exceeded the average market price of the Company's common shares.

**(9) Commitments and Contingencies**

*Eminent Domain Matter*

On approximately March 13, 2018, the Orange County Transportation Authority ("OCTA") filed an eminent domain action against the Company and its Westminster, California, store location to acquire the Company's interest in the property for public purposes related to a transportation project. The Company surrendered possession of this location on approximately January 31, 2019. On March 31, 2020, the Company and representatives of the OCTA agreed to a preliminary settlement of the proceedings, which was formally approved by the OCTA's Board on approximately April 27, 2020. Pursuant to the terms of the settlement, on May 21, 2020, the Company received a cash condemnation settlement from the OCTA in the amount of \$2.5 million for lost profit and property. The Company recorded a pre-tax gain for the \$2.5 million in the second quarter of fiscal 2020 related to the settlement, of which \$0.2 million represented lost property and equipment, which was included as other income in the interim unaudited condensed consolidated statement of operations. Attorneys' fees related to this settlement totaled \$0.1 million in each of fiscal 2020 and 2019 and were included in selling and administrative expense in the interim unaudited condensed consolidated statement of operations.

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On October 6, 2020, the Company reached an agreement and settled a claim with its insurance carrier related to losses incurred in connection with a store previously damaged in a fire. The settlement amount included \$3.5 million for property damage and business interruption. After application of a previous advance of \$0.5 million and deductible of \$0.2 million, the Company expects to receive proceeds of \$2.8 million related to property damage and business interruption. The Company expects to recognize a nonrefundable gain for this amount when the proceeds are received. This gain was contingent and unrealized as of September 27, 2020.

The Company is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters is not expected to have a material adverse effect on the Company's results of operations or financial condition.

**(10) Share-based Compensation**

In April 2019, the Company adopted the 2019 Equity Incentive Plan (the "2019 Plan") and stopped making grants under its 2007 Equity and Performance Incentive Plan, as amended and restated in April 2011 and April 2016 (the "2007 Plan"). As of September 27, 2020, 2,462,604 shares remained available for future grant under the 2019 Plan.

At its discretion, the Company grants share option awards, nonvested share awards and nonvested share unit awards to certain employees, as defined by ASC 718, *Compensation—Stock Compensation*, under the Company's 2019 Plan, and accounts for its share-based compensation in accordance with ASC 718. The Company recognized \$0.4 million and \$1.3 million in share-based compensation expense for the 13 and 39 weeks ended September 27, 2020, respectively, compared to \$0.5 million and \$1.5 million in share-based compensation expense for the 13 and 39 weeks ended September 29, 2019.

*Share Option Awards*

Share option awards granted by the Company generally vest and become exercisable in four equal annual installments of 25% per year with a maximum life of ten years. The exercise price of share option awards is equal to the quoted market price of the Company's common stock on the date of grant. In the first nine months of fiscal 2020, the Company granted 257,000 share option awards with a weighted-average grant-date fair value of \$1.25 per share option award. In the first nine months of fiscal 2019, the Company granted 253,800 share option awards with a weighted-average grant-date fair value of \$1.33 per share option award.

A summary of the status of the Company's share option awards is presented below:

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life (In Years)	Aggregate Intrinsic Value
Outstanding at December 29, 2019	523,150	\$ 5.91		
Granted	257,000	2.23		
Exercised	(5,175)	5.10		
Forfeited or Expired	(5,750)	11.52		
Outstanding at September 27, 2020	<u>769,225</u>	<u>\$ 4.65</u>	<u>8.20</u>	<u>\$ 1,456,503</u>
Exercisable at September 27, 2020	<u>217,612</u>	<u>\$ 7.29</u>	<u>6.94</u>	<u>\$ 131,080</u>
Vested and Expected to Vest at September 27, 2020	<u>756,972</u>	<u>\$ 4.67</u>	<u>8.18</u>	<u>\$ 1,419,456</u>

The aggregate intrinsic value represents the total pretax intrinsic value, based upon the Company's most recent closing stock price of \$5.95 as of September 27, 2020, which would have been received by the share option award holders had all share option award holders exercised their share option awards as of that date.

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The fair value of each share option award on the date of grant is estimated using the Black-Scholes method based on the following weighted-average assumptions:

	13 Weeks Ended		39 Weeks Ended	
	September 27, 2020	September 29, 2019	September 27, 2020	September 29, 2019
Risk-free interest rate	—	1.5%	0.9%	2.5%
Expected term	—	5.7 years	5.7 years	5.7 years
Expected volatility	—	53.0%	63.0%	53.0%
Expected dividend yield	—	10.3%	—	5.1%

The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant for periods corresponding with the expected term of the option award; the expected term represents the weighted-average period of time that option awards granted are expected to be outstanding giving consideration to vesting schedules and historical participant exercise behavior; the expected volatility is based upon historical volatility of the Company's common stock; and the expected dividend yield is based upon the Company's current dividend rate. In order to support its liquidity initiatives throughout the organization as a result of the COVID-19 outbreak, early in the second quarter of fiscal 2020 the Company's Board of Directors suspended its quarterly cash dividend. Due to the uncertainty of future dividend payments when share option awards were granted in the first quarter of fiscal 2020, the Company did not estimate an expected dividend yield assumption for share option awards granted at that time.

As of September 27, 2020, there was \$0.6 million of total unrecognized compensation expense related to share option awards granted. That expense is expected to be recognized over a weighted-average period of 2.7 years.

*Nonvested Share Awards and Nonvested Share Unit Awards*

Nonvested share awards and nonvested share unit awards granted by the Company vest for employees from the date of grant in four equal annual installments of 25% per year. Nonvested share awards and nonvested share unit awards granted by the Company to non-employee directors for their service as directors, as defined by ASC 718, vest 100% on the earlier of (a) the date of the Company's next annual stockholders meeting following the grant date, or (b) the first anniversary of the grant date.

Nonvested share awards become outstanding when granted and are delivered to the recipient upon their vesting. Shares issuable related to nonvested share unit awards, including any dividend reinvestments, are delivered to the recipient on the tenth business day of January following the year in which the recipient's service to the Company is terminated, at which time the units convert to shares and become outstanding. The total fair value of nonvested share awards which vested during the first nine months of fiscal 2020 and 2019 was \$0.4 million and \$0.6 million, respectively. The total fair value of nonvested share unit awards which vested in each of the first nine months of fiscal 2020 and 2019 was \$0.2 million.

The Company granted 321,600 and 308,584 nonvested share awards in the first nine months of fiscal 2020 and 2019, respectively. The weighted-average grant-date fair value per share of the Company's nonvested share awards granted in the first nine months of fiscal 2020 and 2019 was \$1.69 and \$3.34, respectively.

A summary of the status of the Company's nonvested share awards is presented below:

	Shares	Weighted- Average Grant- Date Fair Value
Balance at December 29, 2019	532,524	\$ 6.33
Granted	321,600	1.69
Vested	(240,424)	6.57
Forfeited	(21,110)	4.41
Balance at September 27, 2020	592,590	\$ 3.79

**BIG 5 SPORTING GOODS CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(continued)**

To satisfy employee minimum statutory tax withholding requirements for nonvested share awards that vest, the Company withholds and retires a portion of the vesting common shares, unless an employee elects to pay cash. In the first nine months of fiscal 2020, the Company withheld 64,573 common shares with a total value of \$0.1 million. This amount is presented as a cash outflow from financing activities in the accompanying interim unaudited condensed consolidated statement of cash flows.

The Company granted 40,000 and 72,464 nonvested share unit awards in the first nine months of fiscal 2020 and 2019, respectively. The weighted-average grant-date fair value per share of the Company's nonvested share unit awards granted in the first nine months of fiscal 2020 and 2019 was \$2.28 and \$2.07, respectively.

A summary of the status of the Company's nonvested share unit awards is presented below:

	Units	Weighted- Average Grant- Date Fair Value
Balance at December 29, 2019	75,413	\$ 1.81
Granted	40,000	2.28
Dividend reinvestments	15,168	2.26
Vested	(72,464)	2.07
Dividend reinvestments vested	(17,429)	2.16
Balance at September 27, 2020	<u>40,688</u>	<u>\$ 1.84</u>

As of September 27, 2020, there was \$1.6 million and \$0.1 million of total unrecognized compensation expense related to nonvested share awards and nonvested share unit awards, respectively. That expense is expected to be recognized over a weighted-average period of 2.4 and 0.7 years for nonvested share awards and nonvested share unit awards, respectively.

**(11) Subsequent Events**

On October 22, 2020, the Company's Board of Directors declared a quarterly cash dividend of \$0.10 per share of outstanding common stock, which will be paid on December 15, 2020 to stockholders of record as of December 1, 2020.

As discussed in Note 9 to the Interim Financial Statements, on October 6, 2020, the Company reached an agreement and settled a claim with its insurance carrier related to property damage and business interruption losses incurred in connection with a store previously damaged in a fire, which resulted in a nonrefundable gain in the amount of \$2.8 million that will be recognized upon receipt of the related insurance proceeds. As of September 27, 2020, proceeds were not yet received related to these losses.

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Stockholders and the Board of Directors of  
Big 5 Sporting Goods Corporation  
El Segundo, California

**Results of Review of Interim Financial Information**

We have reviewed the accompanying condensed consolidated balance sheet of Big 5 Sporting Goods Corporation and subsidiaries (the “Company”) as of September 27, 2020, the related condensed consolidated statements of operations and stockholders’ equity for the fiscal 13 and 39 week periods ended September 27, 2020 and September 29, 2019, and of cash flows for the fiscal 39 week periods ended September 27, 2020 and September 29, 2019, and the related notes (collectively referred to as the “interim financial information”). Based on our reviews, we are not aware of any material modifications that should be made to the accompanying interim financial information for it to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated balance sheet of the Company as of December 29, 2019, and the related consolidated statements of operations, stockholders’ equity, and cash flows for the year then ended (not presented herein); and in our report dated February 26, 2020, we expressed an unqualified opinion on those consolidated financial statements and included an explanatory paragraph regarding a change in accounting principle. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 29, 2019, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

**Basis for Review Results**

This interim financial information is the responsibility of the Company’s management. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our reviews in accordance with standards of the PCAOB. A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the PCAOB, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

*/s/ Deloitte & Touche LLP*

Los Angeles, California  
October 28, 2020

## Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of the Big 5 Sporting Goods Corporation (“we,” “our,” “us”) financial condition and results of operations includes information with respect to our plans and strategies for our business and should be read in conjunction with our interim unaudited condensed consolidated financial statements and related notes (“Interim Financial Statements”) included herein, the *Risk Factors* included herein and in our other filings with the Securities and Exchange Commission (“SEC”), and our consolidated financial statements, related notes, *Risk Factors* and *Management’s Discussion and Analysis of Financial Condition and Results of Operations* contained in our Annual Report on Form 10-K for the fiscal year ended December 29, 2019.

Our fiscal year ends on the Sunday nearest December 31. Fiscal 2020 is comprised of 53 weeks and ends on January 3, 2021. Fiscal 2019 was comprised of 52 weeks and ended on December 29, 2019. The first three quarters in fiscal 2020 are each comprised of 13 weeks, and the fourth quarter of fiscal 2020 is comprised of 14 weeks. The four quarters of fiscal 2019 were each comprised of 13 weeks.

### Impact of COVID-19

During March 2020, the World Health Organization declared the rapidly growing novel coronavirus (“COVID-19”) outbreak to be a global pandemic. The COVID-19 pandemic has significantly impacted health and economic conditions throughout the United States, as public concern about becoming ill with the virus has led to the issuance of recommendations and/or mandates from federal, state and local authorities to practice social distancing or self-quarantine.

Beginning on March 20, 2020, we temporarily closed more than one-half of our retail store locations in response to state and local shelter orders related to the COVID-19 outbreak. We were subsequently able to gradually reopen all store locations based initially on qualifying as an “essential” business under applicable regulations and later as a result of the easing of regulatory restrictions on retail operations in our market areas. Additionally, during the second and third fiscal quarters, the pandemic and the shelter orders that were in place in our market areas negatively impacted customer traffic into the stores that were operating. In an effort to promote social distancing protocols, we implemented reduced store hours for our open stores and limited the number of customers in our stores at any one time. While these temporary store closures, limited hours of operation and shelter orders in our market areas related to the COVID-19 outbreak resulted in an overall decrease in same store sales volume in the second quarter of fiscal 2020 of 4.2% compared with the prior year, as we began reopening stores we recognized significant shifts in consumer demand and rapidly evolved our product assortment, and for the second half of the second fiscal quarter our same store sales increased by 15.5% compared to the prior year. This positive sales trending continued into the third quarter of fiscal 2020, leading to same store sales increases of 31.9%, 7.9% and 5.9% in fiscal July, August and September, respectively, for a historically high increase of 14.8% for the third quarter ended September 27, 2020 compared with the prior year. Throughout the third quarter of fiscal 2020 and as of September 27, 2020, all of our stores that were temporarily closed due to COVID-19 had reopened for in-store shopping, subject to continued appropriate social distancing restrictions and with reduced operating hours.

The initial decrease in sales caused by the COVID-19 outbreak caused us to take various actions to enhance our liquidity. On March 27, 2020, we increased borrowings under our \$140.0 million revolving credit facility (the “Credit Facility”) to \$124.3 million. On March 30, 2020, we exercised the accordion feature under our Credit Agreement, which increased the amount available under the Credit Facility to \$165.0 million, and we drew down additional amounts under the Credit Facility that resulted in long-term revolving credit borrowings of \$143.3 million as of March 31, 2020, our highest borrowing level. Additionally, we took measures to reduce expense across the organization, including negotiating lease concessions with landlords that would reduce or defer our lease-related payments, scaling back merchandise inventory orders and extending payment terms with merchandise vendors, implementing temporary and permanent workforce reductions throughout the organization, and reducing advertising and the amount of planned capital spending in fiscal 2020, among other measures. Although a certain portion of these expense reduction initiatives only benefited the second quarter of fiscal 2020, the third quarter of fiscal 2020 continued to reflect labor expense savings due primarily to reduced store operating hours, as well as advertising expense savings due to significantly reduced advertising activity.

In the third quarter of fiscal 2020, we began to resume some normal operating activities, including resuming workforce rehiring, increasing our inventory purchasing activities and resuming rent payments that were previously deferred. During the third quarter, our sales continued to benefit from increased consumer demand for certain product categories as a result of the COVID-19 pandemic, including fitness, outdoor recreation and firearm-related products. This benefit was partially offset by reduced sales in team sports and back-to-school products as a result of limitations on those activities related to COVID-19. Our advertising and promotional programs remained substantially reduced during the third quarter of fiscal 2020 as a result of COVID-19, which has resulted in lower advertising expense and higher profitability.

With our favorable operating results in the second half of the second fiscal quarter and the full third quarter of fiscal 2020, we were able to significantly pay down our debt levels while retaining favorable levels of cash. As of September 27, 2020, we had paid down our long-term revolving credit borrowings to zero, compared to \$124.3 million and \$66.6 million outstanding as of the first quarter ended March 29, 2020 and fiscal year ended December 29, 2019, respectively. As of September 27, 2020, we had cash of \$55.7 million compared to \$44.2 million and \$8.2 million as of the first quarter ended March 29, 2020 and fiscal year ended December 29, 2019, respectively. In response to the strength of our balance sheet, operations and cash flow generation, our Board of Directors reinstated our previously suspended quarterly cash dividend at the previous rate of \$0.05 per share of outstanding common stock. We declared a cash dividend of \$0.10 per share of outstanding common stock, which reflected our reinstated quarterly cash dividend of \$0.05 per share of outstanding common stock for the third quarter of fiscal 2020 and also included an additional \$0.05 per share of outstanding common stock in recognition that we did not pay a dividend in the second quarter of fiscal 2020.

If we are again required to temporarily close a large portion of our stores or we experience a further reduction in store traffic, we may need to take further actions to maintain our operations, including increasing our borrowing levels or suspending dividend payments, depending on how long and to what extent these events impact our business. Additionally, the consumer preferences for certain product categories that have driven positive sales during the COVID-19 pandemic may not continue after the pandemic has subsided, and any change in consumer preferences could negatively impact our results of operations. We may need to increase advertising and promotional activity from the current historically low levels in an effort to drive customer traffic and sales, as well as increase our staffing from the current reduced levels, which could impact profitability.

## Overview

We are a leading sporting goods retailer in the western United States, with 431 stores and an e-commerce platform under the name “Big 5 Sporting Goods” as of September 27, 2020. We provide a full-line product offering in a traditional sporting goods store format that averages approximately 11,000 square feet. Our product mix includes athletic shoes, apparel and accessories, as well as a broad selection of outdoor and athletic equipment for team sports, fitness, camping, hunting, fishing, tennis, golf, winter and summer recreation and roller sports.

The following table summarizes our store count for the periods presented:

	13 Weeks Ended		39 Weeks Ended	
	September 27, 2020	September 29, 2019	September 27, 2020	September 29, 2019
Beginning stores	431	434	434	436
New stores opened	—	—	—	1
Stores permanently closed	—	(1)	(3)	(4)
Ending stores	431	433	431	433

For fiscal 2020, we do not anticipate opening any new stores and we anticipate permanently closing four stores.

## Executive Summary

The favorable increase in net income for the third quarter of fiscal 2020 compared with the third quarter of fiscal 2019 primarily reflected historically-high increased same store sales of 14.8%, combined with initiatives that we implemented earlier this year in response to the COVID-19 pandemic that led to favorable margin impacts, reductions in advertising expense and employee labor expense and other cost savings. The increase in same store sales compares to a 0.3% increase in same store sales for the third quarter of fiscal 2019.

- Net sales for the third quarter of fiscal 2020 increased 14.6% to \$305.0 million compared to \$266.2 million for the third quarter of fiscal 2019. The increase in net sales was primarily attributable to strong consumer demand for various products as a result of the COVID-19 pandemic, which led to an increase in same store sales in the third quarter of fiscal 2020, combined with added sales from new stores opened since June 30, 2019, partially offset by reductions in sales from permanently closed stores. Same store sales increased for our major merchandise category of hardgoods, partially offset by decreases in our categories of footwear and apparel.
- Gross profit for the third quarter of fiscal 2020 represented 36.1% of net sales, compared with 32.3% in the third quarter of the prior year. The increase in gross profit margin resulted mainly from higher merchandise margins and lower store occupancy expense as a percentage of net sales, partially offset by an unfavorable impact from costs capitalized into inventory as a percentage of net sales.

- Selling and administrative expense for the third quarter of fiscal 2020 decreased 7.3% to \$71.3 million, or 23.4% of net sales, compared to \$76.9 million, or 28.9% of net sales, for the third quarter of fiscal 2019. The decrease in selling and administrative expense was primarily attributable to reduced print advertising expense and lower store employee labor and benefit-related expense in connection with actions taken as a response to COVID-19, partially offset by company performance-based incentive accruals.
- Net income for the third quarter of fiscal 2020 was \$28.4 million, or \$1.31 per diluted share, compared to net income of \$6.4 million, or \$0.30 per diluted share, for the third quarter of fiscal 2019. The historically higher earnings were driven primarily by higher net sales and merchandise margins, reduced advertising expense and lower employee labor expense.
- Operating cash flow for the first nine months of fiscal 2020 was a positive \$136.4 million compared to operating cash flow in the first nine months of fiscal 2019 of a positive \$13.7 million, due primarily to decreased funding of merchandise inventory and an increase in net income year over year.
- Capital expenditures for the first nine months of fiscal 2020 decreased to \$5.0 million from \$6.1 million for the first nine months of fiscal 2019.
- Borrowings under the Credit Facility were zero as of September 27, 2020, compared with \$124.3 million, \$66.6 million and \$60.6 million as of March 29, 2020, December 29, 2019 and September 29, 2019, respectively. Our zero borrowings as of September 27, 2020 reflected a full pay-down of the Credit Facility since the end of the first fiscal quarter when, to support our potential additional liquidity needs during the COVID-19 pandemic, we drew down additional amounts under the Credit Facility. We had cash of \$55.7 million as of September 27, 2020, compared to \$44.2 million, \$8.2 million and \$5.0 million as of March 29, 2020, December 29, 2019 and September 29, 2019, respectively.
- We paid cash dividends in the first nine months of fiscal 2020 of \$3.3 million, or \$0.15 per share, compared with \$3.3 million, or \$0.15 per share, in the first nine months of fiscal 2019. As a result of the impact of COVID-19 and as previously announced, our Board of Directors suspended our quarterly cash dividend during the second quarter of fiscal 2020. Our Board of Directors declared a cash dividend of \$0.10 per share during the third quarter of fiscal 2020, which reflected our reinstated quarterly cash dividend of \$0.05 per share of outstanding common stock for the third quarter of fiscal 2020 and also included an additional \$0.05 per share of outstanding common stock in recognition that we did not pay a dividend in the second quarter of fiscal 2020.

## Results of Operations

The results of the interim periods are not necessarily indicative of results for the entire fiscal year.

### 13 Weeks Ended September 27, 2020 Compared to 13 Weeks Ended September 29, 2019

The following table sets forth selected items from our interim unaudited condensed consolidated statements of operations by dollar and as a percentage of our net sales for the periods indicated:

	13 Weeks Ended			
	September 27, 2020		September 29, 2019	
	(Dollars in thousands)			
Net sales	\$ 304,959	100.0%	\$ 266,150	100.0%
Cost of sales (1)	194,924	63.9	180,158	67.7
Gross profit	110,035	36.1	85,992	32.3
Selling and administrative expense (2)	71,337	23.4	76,886	28.9
Operating income	38,698	12.7	9,106	3.4
Interest expense	199	0.1	683	0.3
Income before income taxes	38,499	12.6	8,423	3.1
Income tax expense	10,106	3.3	2,026	0.7
Net income	\$ 28,393	9.3%	\$ 6,397	2.4%

(1) Cost of sales includes the cost of merchandise, net of discounts or allowances earned, freight, inventory reserves, buying, distribution center expense, including depreciation and amortization, and store occupancy expense. Store occupancy expense includes rent, amortization of leasehold improvements, common area maintenance, property taxes and insurance.

(2) Selling and administrative expense includes store-related expense, other than store occupancy expense, as well as advertising, depreciation and amortization, expense associated with operating our corporate headquarters and impairment charges, if any.

*Net Sales.* Net sales increased by \$38.8 million, or 14.6%, to \$305.0 million in the third quarter of fiscal 2020 from \$266.2 million in the third quarter last year. The change in net sales reflected the following:

- Same store sales increased by \$38.7 million, or a historically high 14.8%, for the 13 weeks ended September 27, 2020, versus the comparable 13-week period in the prior year. The increase in same store sales reflected the following:
  - Strong consumer demand for various products as a result of the COVID-19 pandemic, including fitness, outdoor recreation and firearm-related products, led to same store sales increases of 31.9%, 7.9% and 5.9% in fiscal July, August and September, respectively. This benefit was partially offset by reduced sales in team sports and back-to-school products as a result of limitations on those activities related to COVID-19.
  - Sales for our major merchandise category of hardgoods increased, partially offset by decreases in our categories of footwear and apparel.
  - The increase in same store sales compares to a 0.3% increase in same store sales for the third quarter of fiscal 2019.
  - Same store sales for a period normally consist of sales for stores that operated throughout the period and the full corresponding prior-year period, along with sales from e-commerce. Same store sales comparisons exclude sales from stores permanently closed, or stores in the process of closing, during the comparable periods. Sales from e-commerce in the third quarter of fiscal 2020 and 2019 were not material.
- Added sales from new stores opened since June 30, 2019 were offset by a reduction in sales from permanently closed stores.
- We experienced a higher average sale per transaction and decreased customer transactions in the third quarter of fiscal 2020 compared to the same period last year.

*Gross Profit.* Gross profit increased by \$24.0 million to \$110.0 million, or 36.1% of net sales, in the 13 weeks ended September 27, 2020, compared with \$86.0 million, or 32.3% of net sales, in the 13 weeks ended September 29, 2019. The change in gross profit was primarily attributable to the following:

- Net sales increased by \$38.8 million, or 14.6%, compared with the third quarter of last year, primarily attributable to strong consumer demand for various products as a result of the COVID-19 pandemic.
- Merchandise margins, which exclude buying, occupancy and distribution expense, increased by a favorable 277 basis points compared with the third quarter of last year when merchandise margins increased by a favorable 94 basis points. The increase primarily reflects a shift in our product sales mix towards certain higher-margin products, as well as lower promotional activity.
- Distribution expense, including costs capitalized into inventory, increased by \$3.4 million, or an unfavorable 53 basis points, in the third quarter of fiscal 2020 compared to the prior year. The increase primarily reflected lower costs capitalized into inventory corresponding to the decrease in merchandise inventories compared with the third quarter of last year, combined with higher employee labor expense due to increases in our distribution center workforce in order to meet the increased demand for our products.

*Selling and Administrative Expense.* Selling and administrative expense decreased by \$5.6 million to \$71.3 million, or 23.4% of net sales, in the 13 weeks ended September 27, 2020, from \$76.9 million, or 28.9% of net sales, in the third quarter last year. The change in selling and administrative expense was primarily attributable to the following:

- Advertising expense decreased by \$5.8 million, due mainly to lower print advertising in the third quarter of fiscal 2020 that resulted from the impact of the COVID-19 pandemic.
- Store-related expense, excluding occupancy, decreased by \$2.2 million due largely to decreased employee labor and benefit-related expense primarily as a result of reduced store operating hours in response to the COVID-19 pandemic, partially offset by increases in certain other operating expenses, primarily increased insurance premiums. These reductions were partially offset by wage pressures that continue to reflect the incremental impact of legislated minimum wage rate increases primarily in California, where over fifty percent of our stores are located. In April 2016, California passed legislation to enact additional state-wide minimum wage rate increases from \$10.00 to \$15.00 per hour to be implemented in annual increments through fiscal 2022, with annual increases of \$0.50 per hour effective in fiscal 2017 and fiscal 2018, and annual increases of \$1.00 per hour effective in fiscal 2019 through fiscal 2022. Additionally, certain other jurisdictions within California, including Los Angeles and San Francisco, as well as various other states in which we do business, are implementing their own scheduled increases, which may also include interim impacts effective at various points throughout the year. We estimate that the impact of the California state-wide minimum wage rate increase, combined with the impact of the additional minimum wage rate increases in certain other jurisdictions within California and other states, caused our labor expense to increase by approximately \$0.6 million for the third quarter of fiscal 2020 compared with the third quarter of fiscal 2019.

- Administrative expense increased by \$2.5 million, primarily attributable to an increase in company performance-based incentive accruals, partially offset by reductions in various professional services.

*Interest Expense.* Interest expense decreased by \$0.5 million in the third quarter of fiscal 2020 compared to the third quarter of fiscal 2019. Interest expense reflects a decrease in average interest rates and average debt levels that resulted from a full pay-down of borrowings under our Credit Facility in the third quarter of fiscal 2020 compared with the third quarter of fiscal 2019.

*Income Taxes.* The provision for income taxes increased to \$10.1 million for the third quarter of fiscal 2020 from \$2.0 million for the third quarter of fiscal 2019, primarily reflecting higher pre-tax income in the third quarter of fiscal 2020 compared to the third quarter of fiscal 2019. Our effective tax rate was 26.3% for the third quarter of fiscal 2020 and 24.1% for the third quarter of fiscal 2019.

*39 Weeks Ended September 27, 2020 Compared to 39 Weeks Ended September 29, 2019*

The following table sets forth selected items from our interim unaudited condensed consolidated statements of operations by dollar and as a percentage of our net sales for the periods indicated:

	39 Weeks Ended			
	September 27, 2020		September 29, 2019	
	(Dollars in thousands)			
Net sales	\$ 750,630	100.0%	\$ 752,401	100.0%
Cost of sales (1)	503,847	67.1	517,416	68.8
Gross profit	246,783	32.9	234,985	31.2
Selling and administrative expense (2)	201,040	26.8	221,676	29.5
Other income	(2,500)	(0.3)	—	0.0
Operating income	48,243	6.4	13,309	1.7
Interest expense	1,683	0.2	2,197	0.3
Income before income taxes	46,560	6.2	11,112	1.4
Income tax expense	11,642	1.6	3,023	0.4
Net income	\$ 34,918	4.6%	\$ 8,089	1.0%

(1) Cost of sales includes the cost of merchandise, net of discounts or allowances earned, freight, inventory reserves, buying, distribution center expense, including depreciation and amortization, and store occupancy expense. Store occupancy expense includes rent, amortization of leasehold improvements, common area maintenance, property taxes and insurance.

(2) Selling and administrative expense includes store-related expense, other than store occupancy expense, as well as advertising, depreciation and amortization, expense associated with operating our corporate headquarters and impairment charges, if any.

*Net Sales.* Net sales decreased by \$1.8 million, or 0.2%, to \$750.6 million in the first nine months of fiscal 2020 from \$752.4 million in the first nine months last year. The change in net sales reflected the following:

- A reduction in sales from permanently closed stores, including a store temporarily closed for the first half of fiscal 2020 due to a fire, was partially offset by added sales from new stores opened since December 30, 2018 and higher same store sales.
- Same store sales increased by \$3.0 million, or 0.4%, for the 39 weeks ended September 27, 2020, versus the comparable 39-week period in the prior year. The increase in same store sales reflected the following:
  - Due to the COVID-19 pandemic, state and local shelter orders were issued in our various market areas that led to the temporary closure of more than one-half of our stores that began on March 20, 2020 and significantly impacted the first and second fiscal quarters of fiscal 2020, resulting in reduced same store sales versus the prior year. Over the first half of the second fiscal quarter, when the impacts of the COVID-19 pandemic forced us to operate with a significantly reduced store count, our same store sales decreased by 28.2% compared to the prior year period. However, as we began reopening stores, we recognized significant shifts in consumer demand and rapidly evolved our product assortment, and for the second half of the second fiscal quarter our same store sales increased by 15.5% compared to the prior year. This positive sales trending continued into the third quarter of fiscal 2020, with strong consumer demand for various products as a result of the COVID-19 pandemic, including fitness, outdoor recreation and firearm-related products, leading to same store sales increases of 31.9%, 7.9% and 5.9% in fiscal July, August and September, respectively. This benefit was partially offset by reduced sales in team sports and back-to-school products as a result of limitations on those activities related to COVID-19.

- The increase in same store sales was partially offset by the negative impact of challenging winter-weather conditions in the first two months of fiscal 2020 compared with the same period in the prior year. In the first quarter of fiscal 2019, strong sales of winter-related products were driven by highly favorable cold and wet winter weather conditions across our markets compared with warm and dry winter weather conditions this year.
- Sales for our major merchandise category of hardgoods increased, partially offset by decreases in our categories of apparel and footwear.
- The increase in same store sales compares to a 1.8% increase in same store sales for the first nine months of fiscal 2019.
- Same store sales for a period normally consist of sales for stores that operated throughout the period and the full corresponding prior-year period, along with sales from e-commerce. Despite the same store sales increase, our sales for the first nine months ended September 27, 2020 included the impact of sales declines resulting from the temporary store closures that began on March 20, 2020 and negatively impacted the first and second fiscal quarters. Same store sales comparisons exclude sales from stores permanently closed, or stores in the process of closing, during the comparable periods. Sales from e-commerce in the first nine months of fiscal 2020 and 2019 were not material.
- We experienced decreased customer transactions, due primarily to the impact of the COVID-19 outbreak, and a higher average sale per transaction in the first nine months of fiscal 2020 compared to the same period last year.

*Gross Profit.* Gross profit increased by \$11.8 million, or 5.0%, to \$246.8 million, or 32.9% of net sales, in the 39 weeks ended September 27, 2020, from \$235.0 million, or 31.2% of net sales, in the 39 weeks ended September 29, 2019. The change in gross profit was primarily attributable to the following:

- Merchandise margins, which exclude buying, occupancy and distribution expense, increased by a favorable 167 basis points compared with the first nine months of last year when merchandise margins increased by a favorable 9 basis points. The increase primarily reflects a shift in our product sales mix towards certain higher-margin products, as well as lower promotional activity.
- Store occupancy expense decreased by \$2.8 million, or 3.8%, compared with the first nine months of last year primarily as a result of the favorable impact in the second quarter from lease concessions in the amount of \$3.1 million that we negotiated in response to the COVID-19 pandemic.
- Distribution expense, including costs capitalized into inventory, increased by \$4.0 million, or an unfavorable 55 basis points, in the first nine months of fiscal 2020 compared to the prior year. The increase primarily reflected lower costs capitalized into inventory corresponding to the decrease in merchandise inventories compared with the first nine months of last year, partially offset by lower trucking and fuel costs as well as lower employee labor and benefit-related expense due to temporary workforce reductions caused by the COVID-19 pandemic.
- Net sales decreased by \$1.8 million, or 0.2%, compared with the first nine months of last year.

*Selling and Administrative Expense.* Selling and administrative expense decreased by \$20.7 million to \$201.0 million, or 26.8% of net sales, in the 39 weeks ended September 27, 2020, from \$221.7 million, or 29.5% of net sales, in the first nine months of last year. The change in selling and administrative expense was primarily attributable to the following:

- Advertising expense decreased by \$12.9 million, due mainly to lower print advertising in the second and third quarters of fiscal 2020 that resulted from the impact of the COVID-19 pandemic.
- Store-related expense, excluding occupancy, decreased by \$11.7 million, due largely to significantly reduced employee labor and benefit-related expense as a result of temporary workforce reductions and reduced store operating hours in response to the COVID-19 pandemic, as well as decreases in credit card fees and certain other operating expenses, primarily increased insurance premiums.
  - The decrease in employee labor-related expense included an employee retention credit provided by the CARES Act to provide relief for employers subject to closure or significant economic downturn due to the impact of COVID-19, which reduced employee labor-related expense by \$0.9 million for the first nine months of fiscal 2020 compared with the first nine months of fiscal 2019.

- These reductions were partially offset by wage pressures that continue to reflect the incremental impact of legislated minimum wage rate increases primarily in California, where over fifty percent of our stores are located. In April 2016, California passed legislation to enact additional state-wide minimum wage rate increases from \$10.00 to \$15.00 per hour to be implemented in annual increments through fiscal 2022, with annual increases of \$0.50 per hour effective in fiscal 2017 and fiscal 2018, and annual increases of \$1.00 per hour effective in fiscal 2019 through fiscal 2022. Additionally, certain other jurisdictions within California, including Los Angeles and San Francisco, as well as various other states in which we do business, are implementing their own scheduled increases, which may also include interim impacts effective at various points throughout the year. We estimate that the impact of the California state-wide minimum wage rate increase, combined with the impact of the additional minimum wage rate increases in certain other jurisdictions within California and other states, caused our labor expense to increase by approximately \$2.0 million for the first nine months of fiscal 2020 compared with the first nine months of fiscal 2019.
- Administrative expense increased by \$3.9 million primarily attributable to an increase in company performance-based incentive accruals, partially offset by decreases in various other operating expenses that resulted from the impact of the COVID-19 pandemic. Additionally, administrative expense in the first nine months of fiscal 2019 was favorably impacted by a settlement related to the termination of a software contract.

*Other income.* Other income in the first nine months of fiscal 2020 consisted of a cash condemnation settlement related to eminent domain proceedings, as more fully described in Note 9 to the Interim Financial Statements included in Part I, Item 1, *Financial Statements*, of this Quarterly Report on Form 10-Q.

*Interest Expense.* Interest expense decreased by \$0.5 million in the first nine months of fiscal 2020 compared to the first nine months of fiscal 2019. Interest expense reflects a decrease in average interest rates in the first nine months of fiscal 2020 compared with the first nine months of fiscal 2019, partially offset by an increase in average debt levels in the first nine months of fiscal 2020 compared with the first nine months of fiscal 2019. As of the end of the third quarter of fiscal 2020, we had fully paid down borrowings under our Credit Facility to zero.

*Income Taxes.* The provision for income taxes increased to \$11.6 million for the first nine months of fiscal 2020 from \$3.0 million for the first nine months of fiscal 2019, primarily reflecting higher pre-tax income in the first nine months of fiscal 2020 compared to the first nine months of fiscal 2019. Our effective tax rate was 25.0% for the first nine months of fiscal 2020 and 27.2% for the first nine months of fiscal 2019 and reflects the write-off of deferred tax assets related to share-based compensation of \$0.3 million and \$0.4 million in fiscal 2020 and fiscal 2019, respectively. As a result of the CARES Act, we amended our 2018 income tax return and our effective tax rate for the first nine months of fiscal 2020 reflects the carryback of our 2018 net operating loss to a period with a higher statutory income tax rate.

## Liquidity and Capital Resources

Our principal liquidity requirements are for working capital and capital expenditures. We fund our liquidity requirements primarily through cash on hand, cash flows from operations and borrowings from the Credit Facility.

As of September 27, 2020, we had \$55.7 million of cash compared with \$5.0 million as of September 29, 2019. Our cash flows from operating, investing and financing activities are summarized as follows:

	<b>39 Weeks Ended</b>	
	<b>September 27, 2020</b>	<b>September 29, 2019</b>
	<b>(In thousands)</b>	
<b>Total cash provided by (used in):</b>		
Operating activities	\$ 136,388	\$ 13,652
Investing activities	(4,804)	(6,128)
Financing activities	(84,112)	(9,247)
Net increase (decrease) in cash	<u>\$ 47,472</u>	<u>\$ (1,723)</u>

*Operating Activities.* Operating cash flows for the first nine months of fiscal 2020 and 2019 were a positive \$136.4 million and a positive \$13.7 million, respectively. The increased cash flow provided by operating activities for the first nine months of fiscal 2020 compared to the same period last year primarily reflects reduced funding of merchandise inventory caused by the COVID-19 pandemic combined with an increase in net income in fiscal 2020. Additionally, cash flow provided by operating activities included the benefit of higher accrued expense and other liabilities for the first nine months of fiscal 2020 compared with lower accrued expense and other liabilities for the same period of fiscal 2019, primarily related to income taxes, payroll-related expense and rent.

*Investing Activities.* Net cash used in investing activities for the first nine months of fiscal 2020 and 2019 was \$4.8 million and \$6.1 million, respectively. Capital expenditures, excluding non-cash acquisitions, represented cash used in investing activities for each period, and in fiscal 2020 were partially offset by a portion of settlement proceeds from an eminent domain condemnation of \$0.2 million. Capital expenditures for both periods primarily reflect store-related remodeling, distribution center investments and computer hardware and software purchases.

*Financing Activities.* Financing cash flows for the first nine months of fiscal 2020 and 2019 were a negative \$84.1 million and a negative \$9.2 million, respectively. For the first nine months of fiscal 2020 and 2019, net cash was used primarily to pay down borrowings under the Credit Facility, fund dividend payments and make principal payments on finance lease liabilities. The increased cash flow used in financing activities for the first nine months of fiscal 2020 compared to the same period last year primarily reflects a full pay-down of borrowings under the Credit Facility during the second and third fiscal quarters to zero, as a result of improved profitability and cash generation activities in response to the COVID-19 pandemic.

As of September 27, 2020, we had revolving credit borrowings of zero and letter of credit commitments of \$4.7 million outstanding. These balances compare to revolving credit borrowings of \$60.6 million and letter of credit commitments of \$0.5 million outstanding as of September 29, 2019 and revolving credit borrowings of \$66.6 million and letter of credit commitments of \$0.7 million outstanding as of December 29, 2019. Our zero borrowings as of September 27, 2020 reflected a full pay-down of borrowings under the Credit Facility to zero since the first quarter of fiscal 2020 when, to support our potential additional liquidity needs during the COVID-19 pandemic, we drew down additional amounts under the Credit Facility, as discussed in the *Credit Agreement* section below.

In each quarter of fiscal 2019 and the first quarter of fiscal 2020 we paid a quarterly cash dividend of \$0.05 per share of outstanding common stock. In an effort to enhance financial flexibility during the COVID-19 pandemic, we implemented expense reduction and cash preservation initiatives throughout the organization. In connection with that effort, in the second quarter of fiscal 2020 our Board of Directors suspended our quarterly cash dividend. In response to improved strength of our balance sheet, operations and cash flow generation, in the third quarter of fiscal 2020, our Board of Directors reinstated our quarterly cash dividend at the previous rate of \$0.05 per share of outstanding common stock. We declared a cash dividend of \$0.10 per share of outstanding common stock, which was paid on September 15, 2020 to stockholders of record as of September 1, 2020. The \$0.10 cash dividend reflected our reinstated quarterly cash dividend of \$0.05 per share of outstanding common stock for the third quarter of fiscal 2020, and also included an additional \$0.05 per share of outstanding common stock in recognition that we did not pay a dividend in the second quarter of fiscal 2020.

We did not repurchase any shares of common stock in the first nine months of fiscal 2020 or fiscal 2019 pursuant to our current share repurchase program. Since the inception of our initial share repurchase program in May 2006 through September 27, 2020, we have repurchased a total of 3,528,972 shares for \$41.8 million.

*Credit Agreement.* On October 18, 2010, we entered into a credit agreement with Wells Fargo Bank, National Association (“Wells Fargo”), as administrative agent, and a syndicate of other lenders, which was amended on October 31, 2011, December 19, 2013 and September 29, 2017 (as so amended, the “Credit Agreement”), and has a maturity date of September 29, 2022.

The Credit Agreement provides for a Credit Facility with an aggregate committed availability of up to \$140.0 million, which amount may be increased (“accordion feature”) at our option up to a maximum of \$165.0 million. As discussed at the beginning of this *Management’s Discussion and Analysis of Financial Condition and Results of Operations* in the *Impact of COVID-19* section, in order to enhance our financial flexibility and provide liquidity during the COVID-19 pandemic, we exercised the accordion feature under our Credit Agreement and increased the aggregate committed availability under the Credit Facility to \$165.0 million. We may also request additional increases in aggregate availability, up to a maximum of \$200.0 million, in which case the existing lenders under the Credit Agreement will have the option to increase their commitments to accommodate the requested increase. If such existing lenders do not exercise that option, we may (with the consent of Wells Fargo, not to be unreasonably withheld) seek other lenders willing to provide such commitments. The Credit Facility includes a provision which permits us to elect to reduce the aggregate committed availability under the Credit Agreement to \$100.0 million for a three-month period each calendar year. The Credit Facility includes a \$25.0 million sublimit for letters of credit and a \$20.0 million sublimit for swingline loans.

We may borrow under the Credit Facility from time to time, provided the amounts outstanding will not exceed the lesser of the then aggregate availability (as discussed above) and the Borrowing Base (such lesser amount being referred to as the “Loan Cap”). The “Borrowing Base” generally is comprised of the sum, at the time of calculation, of (a) 90.00% of our eligible credit card receivables; plus (b) the cost of our eligible inventory (other than our eligible in-transit inventory), net of inventory reserves, multiplied by 90.00% of the appraised net orderly liquidation value of eligible inventory (expressed as a percentage of the cost of eligible inventory); plus (c) the lesser of (i) the cost of our eligible in-transit inventory, net of inventory reserves, multiplied by 90.00% of the appraised net orderly liquidation value of our eligible in-transit inventory (expressed as a percentage of the cost of eligible in-transit inventory), or (ii) \$10.0 million, minus (d) certain reserves established by Wells Fargo in its role as the Administrative Agent in its reasonable discretion.

Generally, we may designate specific borrowings under the Credit Facility as either base rate loans or LIBO rate loans. The applicable interest rate on our borrowings is a function of the daily average, over the preceding fiscal quarter, of the excess of the Loan Cap over amounts borrowed (such amount being referred to as the “Average Daily Availability”). Those loans designated as LIBO rate loans bear interest at a rate equal to the then applicable adjusted LIBO rate plus an applicable margin as shown in the table below. Those loans designated as base rate loans bear interest at a rate equal to the applicable margin for base rate loans (as shown below) plus the highest of (a) the Federal funds rate, as in effect from time to time, plus one-half of one percent (0.50%), (b) the LIBO rate, plus one percentage point (1.00%), or (c) the rate of interest in effect for such day as announced from time to time within Wells Fargo as its “prime rate.” The applicable margin for all loans is a function of Average Daily Availability for the preceding fiscal quarter as set forth below.

<b>Level</b>	<b>Average Daily Availability</b>	<b>LIBO Rate Applicable Margin</b>	<b>Base Rate Applicable Margin</b>
I	Greater than or equal to \$70,000,000	1.25%	0.25%
II	Less than \$70,000,000	1.375%	0.50%

The commitment fee assessed on the unused portion of the Credit Facility is 0.20% per annum.

Obligations under the Credit Facility are secured by a general lien and perfected security interest in substantially all of our assets. Our Credit Agreement contains covenants that require us to maintain a fixed charge coverage ratio of not less than 1.0:1.0 in certain circumstances, and limit our ability to, among other things, incur liens, incur additional indebtedness, transfer or dispose of assets, change the nature of the business, guarantee obligations, pay dividends or make other distributions or repurchase stock, and make advances, loans or investments. We may declare or pay cash dividends or repurchase stock only if, among other things, no default or event of default then exists or would arise from such dividend or repurchase of stock and, after giving effect to such dividend or repurchase, certain availability and/or fixed charge coverage ratio requirements are satisfied. The Credit Agreement contains customary events of default, including, without limitation, failure to pay when due principal amounts with respect to the Credit Facility, failure to pay any interest or other amounts under the Credit Facility for five days after becoming due, failure to comply with certain agreements or covenants contained in the Credit Agreement, failure to satisfy certain judgments against us, failure to pay when due (or any other default which does or may lead to the acceleration of) certain other material indebtedness in principal amount in excess of \$5.0 million, and certain insolvency and bankruptcy events.

In order to support our liquidity in response to the rapidly growing COVID-19 outbreak, on March 27, 2020, we increased borrowings under our \$140.0 million Credit Facility to \$124.3 million. On March 30, 2020, we exercised the accordion feature under our Credit Agreement and drew down additional amounts under the Credit Facility that resulted in long-term revolving credit borrowings of \$143.3 million as of March 31, 2020, our highest borrowing level. As a result of improved profitability and cash generation activities in response to the COVID-19 pandemic, we paid down to zero our long-term revolving credit borrowings and we had letter of credit commitments of \$4.7 million outstanding as of September 27, 2020, compared with borrowings of \$66.6 million and letter of credit commitments of \$0.7 million as of December 29, 2019. Total remaining borrowing availability, after subtracting letters of credit, was \$160.3 million and \$72.7 million as of September 27, 2020 and December 29, 2019, respectively.

*Future Capital Requirements.* We had cash on hand of \$55.7 million as of September 27, 2020. As a response to the COVID-19 pandemic, we initially suspended capital spending but have since resumed our planned capital spending in fiscal 2020. We now expect capital expenditures for fiscal 2020, excluding non-cash acquisitions, to range from approximately \$6.0 million to \$9.0 million primarily to fund store-related remodeling, distribution center investments and computer hardware and software purchases. For fiscal 2020, we do not anticipate opening any new stores and we anticipate permanently closing four stores.

We have historically paid quarterly cash dividends, subject to declaration by our Board of Directors. In order to support our liquidity initiatives in response to COVID-19, in the second quarter of fiscal 2020 our Board of Directors suspended our quarterly cash dividend. In response to improved strength of our balance sheet, operations and cash flow generation, in the third quarter of fiscal 2020 our Board of Directors reinstated our quarterly cash dividend at the previous rate of \$0.05 per share of outstanding common stock. In the fourth quarter of fiscal 2020 our Board of Directors declared a cash dividend of \$0.10 per share of outstanding common stock, which will be paid on December 15, 2020 to stockholders of record as of December 1, 2020.

As of September 27, 2020, a total of \$15.3 million remained available for share repurchases under our current share repurchase program. We did not repurchase any shares of our common stock in the first nine months of fiscal 2020 or fiscal 2019. We consider several factors in determining when and if we make share repurchases including, among other things, our alternative cash requirements, existing business conditions and the market price of our stock.

We believe we will be able to fund our cash requirements from cash on hand, operating cash flows and borrowings from the Credit Facility, for at least the next 12 months.

*Contractual Obligations.* Our material contractual obligations include operating lease commitments associated with our leased properties and other occupancy expense, finance lease obligations, borrowings under the Credit Facility and other liabilities. Operating lease commitments consist principally of leases for our retail store facilities, distribution center and corporate offices. These leases frequently include options which permit us to extend the terms beyond the initial fixed lease term, and we intend to renegotiate most of these leases as they expire. Operating lease commitments also consist of information technology (“IT”) systems hardware, distribution center delivery tractors and equipment. Additional information regarding our operating and finance leases is available in Notes 2 and 5 to the Interim Financial Statements included in Part I, Item 1, *Financial Statements*, of this Quarterly Report on Form 10-Q.

In the first nine months of fiscal 2020, we paid down to zero our revolving credit borrowings, which decreased by \$66.6 million from the end of fiscal 2019. Our reduced debt levels in fiscal 2020 compared with the prior year end reflect improved profitability and cash generation activities in response to the COVID-19 pandemic in fiscal 2020.

In the ordinary course of business, we enter into arrangements with vendors to purchase merchandise in advance of expected delivery. Because most of these purchase orders do not contain any termination payments or other penalties if cancelled, they are not included as outstanding contractual obligations.

### **Critical Accounting Estimates**

As discussed in Part II, Item 7, *Management’s Discussion and Analysis of Financial Condition and Results of Operations*, of our Annual Report on Form 10-K for the fiscal year ended December 29, 2019, we consider our estimates on operating and finance leases, valuation of inventory and long-lived assets to be among the most critical in understanding the judgments that are involved in preparing our consolidated financial statements. There have been no significant changes to these estimates in the 39 weeks ended September 27, 2020.

### **Seasonality and Impact of Inflation**

We experience seasonal fluctuations in our net sales and operating results. Seasonality in our net sales influences our buying patterns which directly impacts our merchandise inventory and accounts payable levels and cash flows. We purchase merchandise for seasonal activities in advance of a season and supplement our merchandise assortment as necessary and when possible during the season. Our efforts to replenish products during a season are not always successful. In the fourth fiscal quarter, which includes the holiday selling season and the start of the winter selling season, we normally experience higher inventory purchase volumes and increased expense for staffing and advertising. If we miscalculate the consumer demand for our products generally or for our product mix in advance of a season, particularly the fourth quarter, our net sales can decline, which can harm our financial performance. A significant shortfall from expected net sales, particularly during the fourth quarter, can negatively impact our annual operating results.

In fiscal 2019, and during the first nine months of fiscal 2020, the impact of inflation and tariffs on products we purchase was minimal. At the end of fiscal 2019, we brought in certain merchandise early in anticipation of future cost increases. We have evolved our product mix to include more branded merchandise which we believe gives us added flexibility to adjust selling prices for purchase cost increases. If we are unable to adjust our selling prices for purchase cost increases that might occur, then our merchandise margins will decline, which will adversely impact our operating results. We do not believe that inflation or tariffs had a material impact on our operating results for the reporting periods.

## Recently Issued Accounting Updates

See Note 2 to the Interim Financial Statements included in Part I, Item 1, *Financial Statements*, of this Quarterly Report on Form 10-Q.

## Forward-Looking Statements

This document includes certain “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements relate to, among other things, our financial condition, our results of operations, our growth strategy and the business of our company generally. In some cases, you can identify such statements by terminology such as “may,” “could,” “project,” “estimate,” “potential,” “continue,” “should,” “expects,” “plans,” “anticipates,” “believes,” “intends” or other such terminology. These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results to change significantly. These risks and uncertainties include, among other things, the economic impacts of COVID-19 on our business operations, including as a result of regulations that may be issued in response to COVID-19, changes in the consumer spending environment, fluctuations in consumer holiday spending patterns, increased competition from e-commerce retailers, breach of data security or other unauthorized disclosure of sensitive personal or confidential information, the competitive environment in the sporting goods industry in general and in our specific market areas, inflation, product availability and growth opportunities, changes in the current market for (or regulation of) firearm-related products, disruption in product flow, seasonal fluctuations, weather conditions, changes in cost of goods, operating expense fluctuations, increases in labor and benefit-related expense, changes in laws or regulations, including those related to tariffs and duties, public health issues (including those caused by COVID-19), impacts of civil unrest or widespread vandalism, lower than expected profitability of our e-commerce platform or cannibalization of sales from our existing store base which could occur as a result of operating the e-commerce platform, litigation risks, stockholder campaigns and proxy contests, risks related to our historically leveraged financial condition, changes in interest rates, credit availability, higher expense associated with sources of credit resulting from uncertainty in financial markets and economic conditions in general. Those and other risks and uncertainties are more fully described in Part II, Item 1A, *Risk Factors*, in this report and in Part I, Item 1A, *Risk Factors*, in our Annual Report on Form 10-K and other filings with the SEC. We caution that the risk factors set forth in this report and the other reports that we file with the SEC are not exclusive. In addition, we conduct our business in a highly competitive and rapidly changing environment. Accordingly, new risk factors may arise. It is not possible for management to predict all such risk factors, nor to assess the impact of all such risk factors on our business or the extent to which any individual risk factor, or combination of factors, may cause results to differ materially from those contained in any forward-looking statement. We undertake no obligation to revise or update any forward-looking statement that may be made from time to time by us or on our behalf.

## Item 3. Quantitative and Qualitative Disclosures About Market Risk

Because we are a smaller reporting company, as defined by Rule 12b-2 of the Exchange Act, we are not required to provide the information under this Item.

## Item 4. Controls and Procedures

### *Evaluation of Disclosure Controls and Procedures*

We conducted an evaluation, under the supervision and with the participation of our Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”), of the effectiveness of the design and operation of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) as of the end of the period covered by this report. Based on such evaluation, our CEO and CFO have concluded that, as of the end of such period, our disclosure controls and procedures are effective, at a reasonable assurance level, in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act and are effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

### *Changes in Internal Control Over Financial Reporting*

During the fiscal quarter ended September 27, 2020, no changes occurred with respect to our internal control over financial reporting that materially affected, or are reasonably likely to materially affect, internal control over financial reporting.

## PART II. OTHER INFORMATION

### Item 1. Legal Proceedings

The Company is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters is not expected to have a material adverse effect on the Company's results of operations or financial condition.

### Item 1A. Risk Factors

We are providing the following additional risk factor to supplement the risk factors contained in Part I, Item 1A, *Risk Factors*, of our Annual Report on Form 10-K for the fiscal year ended December 29, 2019.

***The novel coronavirus ("COVID-19") pandemic has disrupted and is expected to continue to disrupt our business, which could have a material adverse impact on our business, results of operations, liquidity and financial condition for an extended period of time.***

During March 2020, the World Health Organization declared the rapidly growing COVID-19 outbreak to be a global pandemic. The COVID-19 pandemic has significantly impacted health and economic conditions throughout the United States, as public concern about becoming ill with the virus has led to the issuance of recommendations and/or mandates from federal, state and local authorities to practice social distancing or self-quarantine. Beginning on March 20, 2020, we temporarily closed more than one-half of our retail store locations in response to state and local shelter orders related to the COVID-19 outbreak. We were subsequently able to gradually reopen all of our store locations in some capacity based on either qualifying as an "essential" business under applicable regulations or as a result of the easing of regulatory restrictions on retail operations in our market areas. New temporary closures of stores may be required if additional orders are issued in response to changing health conditions. We have implemented reduced store hours, limited the number of customers in our stores at any one time and have generally implemented social-distancing guidelines throughout our store operating space. As a result of the reduced customer traffic and sales, and in an effort to preserve capital in response to the initial impact of COVID-19, we implemented temporary and permanent workforce reductions throughout the Company, and reduced advertising and planned capital spending in fiscal 2020. We also temporarily reduced merchandise inventory orders, which could impact product availability in our stores and sales in future periods. We may further restrict the operations of our stores and our distribution facility if we deem this necessary or if recommended or mandated by authorities.

As mentioned above, our store locations were considered an "essential" business under applicable regulations in many of the markets in which we operate. In addition, the states and local jurisdictions in which we operate have begun to ease the regulatory restrictions on retail operations that had been put in place with the shelter orders and, as of September 27, 2020 all of our stores that were temporarily closed due to COVID-19 had reopened for in-store shopping, subject to appropriate social distancing restrictions and with reduced operating hours. As our stores have reopened, our sales have benefited from increased consumer demand for certain product categories as a result of the COVID-19 pandemic, including fitness, outdoor recreation and firearm-related products. Additionally, our advertising and promotional activity has been substantially reduced as a result of COVID-19, which has resulted in lower advertising expense and higher profitability.

If the classification of what is an "essential" business changes in jurisdictions where our stores are located, or the restrictions on retail operations in our markets are reinstated, or other government regulations are adopted pertaining to how we may operate our stores, we may be required to temporarily close or restrict operations at more, if not all, of our stores, which would significantly impact our sales and results of operations. Also, if we do not respond appropriately to the pandemic, or if customers do not perceive our response to be adequate for a particular region or our company as a whole, we could suffer damage to our reputation and our brand, which could adversely affect our business in the future.

COVID-19 has also impacted our supply chain for products we sell, particularly those products that are sourced from China. To the extent one or more of our vendors is negatively impacted by COVID-19, including due to the closure of its distribution centers or manufacturing facilities, we may be unable to maintain delivery schedules or adequate inventory in our stores.

The extent to which the COVID-19 outbreak impacts our business, results of operations, liquidity and financial condition will depend on future developments, which are highly uncertain and cannot be predicted, including, but not limited to the duration, spread, severity and impact of the COVID-19 outbreak, the effects of the outbreak on our customers, employees and vendors, the regulatory response and impact of stimulus measures adopted by local, state and federal governments, and to what extent normal economic and operating conditions can resume. Even after the COVID-19 outbreak has subsided, we could experience materially adverse impacts to our business as a result of any economic recession or depression that has occurred or may occur in the future due to a continued erosion in consumer sentiment or the effect of high unemployment on our consumer base. Additionally, the consumer preferences for certain product categories that have driven positive sales during the COVID-19 outbreak may not continue after the outbreak has subsided, and any change in consumer preferences could negatively impact our results of operations. We may need to increase advertising and promotional activity from the current historically low levels in an effort to drive customer traffic and sales, which could impact our profitability. As business conditions evolve, we may need to increase our staffing from the current reduced levels, which could impact profitability. Furthermore, the financial condition of our customers and vendors may be adversely impacted by the pandemic, which may result in a decrease in discretionary consumer spending and our store traffic and sales, and an increase in bankruptcies or insolvencies with respect to our vendors. These events may, in turn, have a material adverse impact on our business, results of operations, liquidity and financial condition. In the event of a prolonged material economic downturn, including circumstances that require us to close a large portion of our stores or cause us to experience a further reduction in store traffic, we may not be able to comply with the financial covenants in our Credit Facility, which could negatively impact our ability to borrow under that facility or with other lenders, negatively impact our liquidity position and may increase our risk of insolvency.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

Not applicable.

**Item 3. Defaults Upon Senior Securities**

Not applicable.

**Item 4. Mine Safety Disclosures**

Not applicable.

**Item 5. Other Information**

Not applicable.

**Item 6. Exhibits**

(a) Exhibits

<b>Exhibit Number</b>	<b>Description of Document</b>
15.1	<a href="#">Independent Auditors' Awareness Letter Regarding Interim Financial Statements.</a> (1)
31.1	<a href="#">Rule 13a-14(a) Certification of Chief Executive Officer.</a> (1)
31.2	<a href="#">Rule 13a-14(a) Certification of Chief Financial Officer.</a> (1)
32.1	<a href="#">Section 1350 Certification of Chief Executive Officer.</a> (1)
32.2	<a href="#">Section 1350 Certification of Chief Financial Officer.</a> (1)
101.INS	XBRL Instance Document. (1)
101.SCH	XBRL Taxonomy Extension Schema Document. (1)
101.CAL	XBRL Taxonomy Calculation Linkbase Document. (1)
101.DEF	XBRL Taxonomy Definition Linkbase Document. (1)
101.LAB	XBRL Taxonomy Label Linkbase Document. (1)
101.PRE	XBRL Taxonomy Presentation Linkbase Document. (1)

(1) Filed herewith.



October 28, 2020

The Board of Directors and Stockholders of Big 5 Sporting Goods Corporation  
2525 East El Segundo Boulevard  
El Segundo, CA 90245

We are aware that our report dated October 28, 2020, on our review of the interim financial information of Big 5 Sporting Goods Corporation and subsidiaries appearing in this Quarterly Report on Form 10-Q for the quarter ended September 27, 2020, is incorporated by reference in Registration Statement Nos. 333-149730, 333-179602, 333-215545, and 333-234317 each on Form S-8.

/s/ Deloitte & Touche LLP

Los Angeles, California

## CERTIFICATIONS

I, Steven G. Miller, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Big 5 Sporting Goods Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: October 28, 2020

/s/ Steven G. Miller  
\_\_\_\_\_  
Steven G. Miller  
President and Chief Executive Officer

## CERTIFICATIONS

I, Barry D. Emerson, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Big 5 Sporting Goods Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: October 28, 2020

/s/ Barry D. Emerson  
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Barry D. Emerson  
Senior Vice President, Chief Financial Officer and Treasurer

**CERTIFICATION**  
**PURSUANT TO 18 U.S.C. SECTION 1350,**  
**AS ADOPTED PURSUANT TO SECTION 906 OF**  
**THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Big 5 Sporting Goods Corporation (the "Company") for the period ending September 27, 2020 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Steven G. Miller, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Steven G. Miller  
Steven G. Miller  
President and Chief Executive Officer

October 28, 2020

A signed original of this written statement required by Section 906 has been provided to Big 5 Sporting Goods Corporation and will be retained by Big 5 Sporting Goods Corporation and furnished to the Securities and Exchange Commission or its staff upon request.

**CERTIFICATION**  
**PURSUANT TO 18 U.S.C. SECTION 1350,**  
**AS ADOPTED PURSUANT TO SECTION 906 OF**  
**THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Big 5 Sporting Goods Corporation (the “Company”) for the period ending September 27, 2020 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Barry D. Emerson, Senior Vice President, Chief Financial Officer and Treasurer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Barry D. Emerson  
Barry D. Emerson  
Senior Vice President, Chief Financial Officer and Treasurer

October 28, 2020

A signed original of this written statement required by Section 906 has been provided to Big 5 Sporting Goods Corporation and will be retained by Big 5 Sporting Goods Corporation and furnished to the Securities and Exchange Commission or its staff upon request.