KOHLS Corp
Form 10-Q
December 06, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
(Mark One)

ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended November 2, 2013

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 1-11084

KOHL'S CORPORATION
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Wisconsin | 39-1630919 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| N56 W17000 Ridgewood Drive, Menomonee Falls, Wisconsin | 53051 |
| (Address of principal executive offices) | (Zip Code) |

Registrant's telephone number, including area code (262) 703-7000

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 ý No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted 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 and post such files). Yes ý No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

| | | | |
|---|---|---|---|
| Large accelerated filer | ý | Accelerated filer | ¨ |
| Non-accelerated filer | ¨¬ (Do not check if a smaller reporting company) | Smaller reporting company | ¨ |

Indicate by a check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes ¨ No ý
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: November 30, 2013 Common Stock, Par Value $0.01 per Share, 214,139,923 shares outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

KOHL'S CORPORATION
CONSOLIDATED BALANCE SHEETS
(In Millions)

| Assets | November 2, 2013 (Unaudited) | February 2, 2013 (Audited) | October 27, 2012 (Unaudited) |
|---|---|---|---|
| Current assets: | | | |
| Cash and cash equivalents | $ 598 | $ 537 | $ 550 |
| Merchandise inventories | 4,959 | 3,748 | 4,851 |
| Deferred income taxes | 147 | 122 | 124 |
| Other | 283 | 312 | 281 |
| Total current assets | 5,987 | 4,719 | 5,806 |
| Property and equipment, net | 8,925 | 8,872 | 9,009 |
| Long-term investments | 57 | 53 | 90 |
| Other assets | 276 | 261 | 256 |
| Total assets | $ 15,245 | $ 13,905 | $ 15,161 |
| | | | |
| Liabilities and Shareholders' Equity | | | |
| Current liabilities: | | | |
| Accounts payable | $ 2,261 | $ 1,307 | $ 2,429 |
| Accrued liabilities | 1,198 | 986 | 1,127 |
| Income taxes payable | 41 | 137 | 48 |
| Current portion of capital lease and financing obligations | 141 | 105 | 100 |
| Total current liabilities | 3,641 | 2,535 | 3,704 |
| Long-term debt | 2,792 | 2,492 | 2,492 |
| Capital lease and financing obligations | 1,950 | 1,956 | 1,986 |
| Deferred income taxes | 390 | 362 | 395 |
| Other long-term liabilities | 548 | 512 | 478 |
| Shareholders' equity: | | | |
| Common stock | 4 | 4 | 4 |
| Paid-in capital | 2,557 | 2,454 | 2,423 |
| Treasury stock, at cost | (7,802) | (7,243) | (6,848) |
| Accumulated other comprehensive loss | (39) | (45) | (48) |
| Retained earnings | 11,204 | 10,878 | 10,575 |
| Total shareholders' equity | 5,924 | 6,048 | 6,106 |
| Total liabilities and shareholders' equity | $ 15,245 | $ 13,905 | $ 15,161 |

See accompanying Notes to Consolidated Financial Statements

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KOHL'S CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)
(In Millions, Except per Share Data)

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | November 2, 2013 | October 27, 2012 | November 2, 2013 | October 27, 2012 |
| Net sales | $4,444 | $4,490 | $12,932 | $12,937 |
| Cost of merchandise sold (exclusive of depreciation shown separately below) | 2,778 | 2,778 | 8,063 | 8,059 |
| Gross margin | 1,666 | 1,712 | 4,869 | 4,878 |
| Operating expenses: | | | | |
| Selling, general, and administrative | 1,073 | 1,077 | 3,071 | 3,055 |
| Depreciation and amortization | 228 | 210 | 665 | 620 |
| Operating income | 365 | 425 | 1,133 | 1,203 |
| Interest expense, net | 84 | 80 | 251 | 243 |
| Income before income taxes | 281 | 345 | 882 | 960 |
| Provision for income taxes | 104 | 130 | 327 | 351 |
| Net income | $177 | $215 | $555 | $609 |
| Net income per share: | | | | |
| Basic | $0.82 | $0.92 | $2.53 | $2.56 |
| Diluted | $0.81 | $0.91 | $2.51 | $2.54 |
| Dividends declared and paid per share | $0.35 | $0.32 | $1.05 | $0.96 |

See accompanying Notes to Consolidated Financial Statements

KOHL'S CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)
(In Millions)

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | November 2, 2013 | October 27, 2012 | November 2, 2013 | October 27, 2012 |
| Net income | $177 | $ 215 | $555 | $ 609 |
| Other comprehensive income, net of tax: | | | | |
| Unrealized gains on investments | — | 3 | 4 | 3 |
| Reclassification adjustment for interest expense on interest rate derivative included in net income | 1 | 1 | 2 | 2 |
| Other comprehensive income | 1 | 4 | 6 | 5 |
| Comprehensive income | $178 | $ 219 | $561 | $ 614 |

See accompanying Notes to Consolidated Financial Statements

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KOHL'S CORPORATION
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(Unaudited)
(In Millions, Except per Share Data)

| | Common Stock | | Paid-In Capital | Treasury Stock | | Accumulated Other Comprehensive Loss | Retained Earnings | Total |
|---|---|---|---|---|---|---|---|---|
| | Shares | Amount | | Shares | Amount | | | |
| Balance at February 2, 2013 | 360 | $4 | $2,454 | (138) | $(7,243) | $(45) | $10,878 | $6,048 |
| Comprehensive income | — | — | — | — | — | 6 | 555 | 561 |
| Stock options and awards | 3 | — | 120 | — | — | — | — | 120 |
| Net income tax impact from stock-based compensation | — | — | (17) | — | — | — | — | (17) |
| Dividends paid ($1.05 per common share) | — | — | — | — | 3 | — | (229) | (226) |
| Treasury stock purchases | — | — | — | (11) | (562) | — | — | (562) |
| Balance at November 2, 2013 | 363 | $4 | $2,557 | (149) | $(7,802) | $(39) | $11,204 | $5,924 |

See accompanying Notes to Consolidated Financial Statements

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KOHL'S CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In Millions)

| | Nine Months Ended | |
| --- | --- | --- |
| | November 2, 2013 | October 27, 2012 |
| Operating activities | | |
| Net income | $555 | $609 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 665 | 620 |
| Share-based compensation | 41 | 37 |
| Excess tax benefits from share-based compensation | (3) | (3) |
| Deferred income taxes | (1) | (46) |
| Other non-cash revenues and expenses | 30 | 26 |
| Changes in operating assets and liabilities: | | |
| Merchandise inventories | (1,204) | (1,628) |
| Other current and long-term assets | 11 | 30 |
| Accounts payable | 954 | 1,196 |
| Accrued and other long-term liabilities | 79 | (47) |
| Income taxes | (113) | (91) |
| Net cash provided by operating activities | 1,014 | 703 |
| Investing activities | | |
| Acquisition of property and equipment | (465) | (641) |
| Sales of investments in auction rate securities | 1 | 68 |
| Other | 13 | 5 |
| Net cash used in investing activities | (451) | (568) |
| Financing activities | | |
| Treasury stock purchases | (562) | (883) |
| Dividends paid | (229) | (227) |
| Proceeds from issuance of debt | 300 | 350 |
| Proceeds from financing obligations | — | 7 |
| Capital lease and financing obligation payments | (87) | (87) |
| Proceeds from stock option exercises | 77 | 50 |
| Excess tax benefits from share-based compensation | 3 | 3 |
| Deferred financing costs | (4) | (3) |
| Net cash used in financing activities | (502) | (790) |
| Net increase (decrease) in cash and cash equivalents | 61 | (655) |
| Cash and cash equivalents at beginning of period | 537 | 1,205 |
| Cash and cash equivalents at end of period | $598 | $550 |
| Supplemental information: | | |
| Interest paid, net of capitalized interest | $221 | $207 |
| Income taxes paid | 438 | 490 |
| Non-Cash Investing and Financing Activities | | |
| Property and equipment acquired through additional liabilities | $119 | $60 |

See accompanying Notes to Consolidated Financial Statements

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KOHL'S CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for fiscal year end financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. For further information, refer to the financial statements and related footnotes included in our Annual Report on Form 10-K for the fiscal year ended February 2, 2013 (Commission File No. 1-11084) as filed with the Securities and Exchange Commission on March 22, 2013.

Due to the seasonality of our business, results for any quarter are not necessarily indicative of the results that may be achieved for a full fiscal year. In addition, quarterly results of operations may be impacted by the timing and amount of sales and costs associated with the opening of new stores.

We operate as a single business unit.

To conform to the current year presentations, we have corrected the presentation of $33 million of deferred revenues that were previously recorded as a reduction to merchandise inventory as of October 27, 2012.

2. Debt

Long-term debt consists of the following unsecured senior debt:

| Maturity | Effective Rate | | Coupon Rate | | Outstanding November 2, 2013 | | February 2, 2013 and October 27, 2012 | |
|---|---|---|---|---|---|---|---|---|
| | | | | | (Dollars in Millions) | | | |
| 2017 | 6.31 | % | 6.25 | % | $650 | | $650 | |
| 2021 | 4.81 | % | 4.00 | % | 650 | | 650 | |
| 2023 | 3.25 | % | 3.25 | % | 350 | | 350 | |
| 2023 | 4.78 | % | 4.75 | % | 300 | | — | |
| 2029 | 7.36 | % | 7.25 | % | 200 | | 200 | |
| 2033 | 6.05 | % | 6.00 | % | 300 | | 300 | |
| 2037 | 6.89 | % | 6.00 | % | 350 | | 350 | |
| | 5.54 | % | | | 2,800 | | 2,500 | |
| Unamortized debt discount | | | | | (8 | ) | (8 | ) |
| Long-term debt | | | | | $2,792 | | $2,492 | |

In September 2013, we issued $300 million of4.75% notes with semi-annual interest payments beginning December 2013. The notes mature on December 2023.

3. Fair Value Measurements

ASC No. 820, "Fair Value Measurements and Disclosures," requires fair value measurements be classified and disclosed in one of the following pricing categories:

Level 1: Financial instruments with unadjusted, quoted prices listed on active market exchanges.

Level 2: Financial instruments lacking unadjusted, quoted prices from active market exchanges, including over-the-counter traded financial instruments. The prices for the financial instruments are determined using prices for recently traded financial instruments with similar underlying terms as well as directly or indirectly observable inputs, such as interest rates and yield curves that are observable at

| | |
|---|---|
| | commonly quoted intervals. |
| Level 3: | Financial instruments that are not actively traded on a market exchange. This category includes situations where there is little, if any, market activity for the financial instrument. The prices are determined using significant unobservable inputs or valuation techniques. |

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KOHL'S CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following table summarizes our financial instruments:

| | | November 2, 2013 | | February 2, 2013 | | October 27, 2012 | |
|---|---|---|---|---|---|---|---|
| | Pricing Category | Cost | Fair Value | Cost | Fair Value | Cost | Fair Value |
| | | (In Millions) | | | | | |
| Cash and cash equivalents | Level 1 | $598 | $598 | $537 | $537 | $550 | $550 |
| Long-term investments | Level 3 | 82 | 57 | 84 | 53 | 124 | 90 |
| Debt | Level 1 | 2,792 | 2,960 | 2,492 | 2,702 | 2,492 | 2,894 |

Our long-term investments consist primarily of investments in auction rate securities ("ARS"). The fair values for our ARS were based on third-party pricing models which utilized a discounted cash flow model for each of the securities as there was no recent activity in the secondary markets in these types of securities. This model used a combination of observable inputs which were developed using publicly available market data obtained from independent sources and unobservable inputs that reflect our own estimates of the assumptions that market participants would use in pricing the investments. Observable inputs include interest rate currently being paid, maturity and credit ratings.

Unobservable inputs include expected redemption date and discount rate. We assumed a seven-year redemption period in valuing our ARS. We intend to hold our ARS until maturity or until we can liquidate them at par value. Based on our other sources of income, we do not believe we will be required to sell them before recovery of par value. In some cases, holding the security until recovery may mean until maturity, which ranges from 2037 to 2039. The discount rate was calculated using the closest match available for other insured asset backed securities. Discount rates ranged from 6.57% to 9.47%. The weighted-average discount rate was 7.64%. A market failure scenario was employed as recent successful auctions of these securities were very limited. Assuming a longer redemption period and a higher discount rate would result in a lower fair market value. Similarly, assuming a shorter redemption period and a lower discount rate would result in a higher fair market value.

The following table presents a rollforward of our long-term investments:

| | Nine Months Ended | |
|---|---|---|
| | November 2, 2013 | October 27, 2012 |
| | (In Millions) | |
| Balance at beginning of year | $53 | $153 |
| Sales | (2) | (68) |
| Unrealized gains | 6 | 5 |
| Balance at end of period | $57 | $90 |

4. Stock-Based Compensation

The following table summarizes our stock-based compensation expense:

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | November 2, 2013 | October 27, 2012 | November 2, 2013 | October 27, 2012 |
| | (In Millions) | | | |
| Stock options | $4 | $5 | $13 | $22 |
| Restricted shares | 10 | 8 | 28 | 15 |
| Total stock-based compensation expense | $14 | $13 | $41 | $37 |

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KOHL'S CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following table summarizes stock-based compensation grants:

| | Nine Months Ended | |
|---|---|---|
| | November 2, 2013 | October 27, 2012 |
| | (In Thousands) | |
| Stock options granted | 549 | 1,387 |
| Restricted shares granted, excluding shares earned in lieu of cash dividends | 873 | 1,001 |
| Total stock-based compensation grants | 1,422 | 2,388 |
| Weighted average fair value at grant date: | | |
| Stock options | $10.57 | $11.84 |
| Restricted shares | $47.97 | $49.00 |

5. Contingencies

We are subject to certain legal proceedings and claims arising out of the conduct of our business. In the opinion of management, the outcome of these proceedings and litigation will not have a material adverse impact on our consolidated financial statements.

6. Net Income Per Share

The following table summarizes our basic and diluted net income per share calculations:

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | November 2, 2013 | October 27, 2012 | November 2, 2013 | October 27, 2012 |
| | (In Millions) | | | |
| Numerator—Net income | $177 | $215 | $555 | $609 |
| Denominator—Weighted average shares: | | | | |
| Basic | 216 | 233 | 219 | 238 |
| Impact of dilutive employee stock options | 2 | 2 | 2 | 2 |
| Diluted | 218 | 235 | 221 | 240 |
| Antidilutive shares | 8 | 9 | 12 | 13 |

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

For purposes of the following discussion, all references to “the quarter” and “the third quarter” are for the 13-week fiscal periods ended November 2, 2013 and October 27, 2012 and all references to "year to date" are for the 39-week fiscal periods ended November 2, 2013 and October 27, 2012.
The following discussion should be read in conjunction with our Consolidated Financial Statements and the related notes included elsewhere in this report, as well as the financial and other information included in our 2012 Annual Report on Form 10-K (our “2012 Form 10-K”). The following discussion may contain forward-looking statements that reflect our plans, estimates and beliefs. Our actual results could materially differ from those discussed in these forward-looking statements. Factors that could cause or contribute to those differences include, but are not limited to, those discussed elsewhere in this report and in our 2012 Form 10-K (particularly in “Risk Factors”).

Executive Summary

As of November 2, 2013, we operated 1,158 family-oriented department stores and a website (www.Kohls.com) that sell moderately priced apparel, footwear and accessories for women, men and children; soft home products such as sheets and pillows; and housewares. Our product offerings include quality private and exclusive brands which are found “Only at Kohl’s” as well as national brands which appeal to classic, modern classic and contemporary customers. Our stores generally carry a consistent merchandise assortment with some differences attributable to regional preferences. Our website includes merchandise which is available in our stores, as well as merchandise which is available only on-line.
The following table summarizes our results for the quarter and year to date:

| | Quarter | Year to Date |
|---|---|---|
| | (Dollars in Millions) | |
| Net sales | $4,444 | $12,932 |
| Change in: | | |
| Net sales | (1.0)% | —% |
| Comparable store sales | (1.6)% | (0.9)% |
| Gross margin as a percent of net sales | 37.5% | 37.7% |
| Selling, general and administrative expenses | $1,073 | $3,071 |
| Net income | $177 | $555 |
| Net earnings per diluted share | $0.81 | $2.51 |
| Shares repurchased (In Millions) | 5.3 | 10.8 |
| Treasury stock purchases | $283 | $562 |

Our main business objective is to profitably increase sales. In order to increase sales, we believe that we need to continue to improve the quality of our merchandise and to offer items at great values. We are pleased with the progress we have made in these areas, but believe that we need to continue to progress in order to increase transactions per store, which is our primary sales driver.

We expanded our loyalty program to California and the Pittsburgh market during the third quarter. Including Texas and the original test markets, the program is now available to customers in almost 30% of our stores. The loyalty program allows enrolled customers to earn various rewards or discounts based upon the volume of their purchases. Initial results have shown a low single-digit sales increase in loyalty markets when compared to similar control markets. We continue to review the results of these pilots and modify earning thresholds, redemption time frames, in-store communication and other elements of the program. We believe that over the long-term, the loyalty program could be a powerful tool to increase customer traffic and sales.

Approximately 280 stores have renovated beauty departments. We are testing three different beauty renovations - new fixtures with expanded and/or relocated floor space, new fixtures with no change to department size or location, and existing fixtures with acrylic retrofits. Initial test results are showing a significant increase in beauty sales in the renovated stores.

We opened 12 new stores during the first nine months of 2013 and plan to open approximately 10 new stores in 2014. Substantially all of the new stores opened in 2013 and expected to open in 2014 are "small" stores with less than 64,000 square

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feet of retail space. We remodeled 30 stores this year and expect to remodel between 35 and 50 stores in 2014. Final remodel decisions will be based on the results of our beauty tests and other remodel concepts that we are testing.
We continue to focus on creating excitement for our customers to increase customer traffic to our stores and website. In fiscal 2014, we expect to launch several new brands, including Juicy Couture, IZOD, and a Jumping Beans collection featuring Disney characters. The Juicy Couture assortment will include women's and girl's apparel, footwear, accessories, bedding, and home accessories. The IZOD assortment will feature men's sportswear and dress apparel, including golf separates, woven sport shirts, sweaters, knit shirts, shorts, suit separates, dress shirts, and dress pants.

Even though our third quarter sales were lower than planned, we were able to effectively manage inventory purchases and, as a result, believe our inventory levels and composition are appropriate as we enter the fourth quarter.

We remain committed to meeting the changing shopping needs of our customer, to strengthening our omni-channel experience and to investing in our future in a strategic and profitable manner.

Results of Operations

Net sales.

Comparable store sales include sales for stores (including relocated or remodeled stores) which were open during both the current and prior year periods. We also include E-Commerce sales in our comparable store sales. Omni-channel sales are recorded as store or E-Commerce sales based on the fulfillment channel. For example, customer purchases from our in-store kiosks are generally recognized as E-Commerce sales as the orders are shipped from our E-Commerce fulfillment centers and on-line orders which are shipped from our stores are recognized as store sales. Merchandise returns reduce sales at the location of the return. As a result, store sales are reduced by merchandise purchased on-line, but returned to a store.

The following tables summarize sales and the changes in sales:

| | Quarter | | Year to Date | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| | (Dollars in Millions) | | | |
| Net Sales | $4,444 | $4,490 | $12,932 | $12,937 |

| | Quarter | | Year to Date | |
|---|---|---|---|---|
| Increase (decrease): | $ | % | $ | % |
| Comparable store sales: | (Dollars in Millions) | | | |
| Stores | $(116) | (2.8)% | $(303) | (2.5)% |
| E-Commerce | 44 | 14.9 | 188 | 24.1 |
| Total | (72) | (1.6) | (115) | (0.9) |
| New stores and other revenues | 26 | — | 110 | — |
| Total decrease in net sales | $(46) | (1.0)% | $(5) | —% |

Drivers of the changes in comparable store sales were as follows:

| | Quarter | Year to Date |
|---|---|---|
| Selling price per unit | (1.9)% | (2.3)% |
| Units per transaction | 1.1 | 2.7 |
| Average transaction value | (0.8) | 0.4 |
| Number of transactions | (0.8) | (1.3) |
| Comparable store sales | (1.6)% | (0.9)% |

The decreases in selling price per unit were primarily due to clearance merchandise which represented a higher percentage of our total sales and was sold at slightly deeper discounts than in the prior year periods. Units per transaction increased as customers purchased more items in response to the lower prices. Increases in the number of E-Commerce transactions were more than offset by decreases in our stores. Year-to-date transactions were also negatively impacted by an unseasonably cold spring which reduced customer visits early in the year.

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The West region reported the strongest comparable store sales for both the quarter and year to date. The remaining regions all reported low to mid single-digit decreases. The Southeast and South Central regions reported the largest comparable store sales decreases for the quarter. Year to date, the Mid-Atlantic region had the largest comparable store sales decrease.

E-Commerce revenues totaled $339 million for the quarter and $970 million year to date. Our E-Commerce revenues increased over both prior year periods, but at rates which were slower than our historical growth rates. We replaced our E-Commerce platform in the second quarter of 2013. As expected, this resulted in a temporary deceleration in our E-Commerce growth in the second and third quarters of 2013. We expect E-Commerce growth to re-accelerate in the fourth quarter.

For the quarter, Accessories was the best performing line of business. Beauty led the Accessories business and reflects the positive impacts of our beauty remodel program and new brand launches. Home, Men's and Women's also outperformed the Company. Notable Home categories included bedding, luggage, electrics and other soft home categories such as rugs and pillows. Men's and Women's both reported higher comparable store sales in the active category. Children's and Footwear were below the Company average. Infant/toddlers reported the lowest sales decrease in the Children's business and athletic shoes reported the highest sales increase in the Footwear business. Year to date, Children's and Home reported the lowest comparable store sales decreases. Men's also outperformed the Company average. Footwear, Women's and Accessories were slightly below the Company average. Notable sales increases were reported in Men's tailored & dress, Women's active/fitness, beauty Accessories and athletic Footwear. In the Home business, electrics and luggage reported the highest sales increases, and toys reported the highest sales increases in Children's.

Gross margin.

Gross margin includes the total cost of products sold, including product development costs, net of vendor payments other than reimbursement of specific, incremental and identifiable costs; inventory shrink; markdowns; freight expenses associated with moving merchandise from our vendors to our distribution centers; shipping and handling expenses of E-Commerce sales; and terms cash discount. Our gross margin may not be comparable with that of other retailers because we include distribution center costs in selling, general and administrative expenses while other retailers may include these expenses in cost of merchandise sold.

The following table summarizes gross margin as a percent of sales:

| | Quarter | | | Year to Date | | |
|---|---|---|---|---|---|---|
| | 2013 | 2012 | Decrease | 2013 | 2012 | Increase (Decrease) |
| Merchandise margin | 38.2 % | 38.7 % | (57) bp | 38.3 % | 38.3 % | 2 bp |
| Shipping impact | (0.7 ) | (0.6 ) | (7 ) | (0.6 ) | (0.6 ) | (6 ) |
| Gross margin | 37.5 % | 38.1 % | (64) bp | 37.7 % | 37.7 % | (4) bp |

The decreases in merchandise margin reflect higher markdowns. E-Commerce growth resulted in slightly higher shipping loss impacts.

E-Commerce decreased our gross margin rate by approximately 80 basis points for the quarter and 70 basis points year to date. Our E-Commerce business currently has a lower gross margin than our stores due to the mix of products sold on-line and free or related shipping promotions. As our E-Commerce business has grown, it has had a more significant impact on our overall gross margin results.

Selling, general and administrative expenses.

| | Quarter | Year to Date |
|---|---|---|

| | 2013 | 2012 | Decrease $ | % | 2013 | 2012 | Increase $ | % |
|---|---|---|---|---|---|---|---|---|
| | (Dollars in Millions) | | | | | | | |
| Selling, general and administrative expenses | $1,073 | $1,077 | $(4) | — % | $3,071 | $3,055 | $16 | 1 % |
| As a percent of net sales | 24.1 % | 24.0 % | | | 23.7 % | 23.6 % | | |

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Selling, general and administrative expenses ("SG&A") include compensation and benefit costs (including stores, headquarters, buying and merchandising and distribution centers); occupancy and operating costs of our retail, distribution and corporate facilities; freight expenses associated with moving merchandise from our distribution centers to our retail stores and among distribution and retail facilities; marketing expenses, offset by vendor payments for reimbursement of specific, incremental and identifiable costs; net revenues from our Kohl's credit card operations; and other administrative revenues and expenses. SG&A also includes the costs incurred prior to new store openings, such as advertising, hiring and training costs for new employees, processing and transporting initial merchandise, and rent expense. We do not include depreciation and amortization in SG&A. The classification of these expenses varies across the retail industry.

The following table summarizes the changes in SG&A by expense type:

| | Quarter | Year to Date |
|---|---|---|
| | (In Millions) | |
| Store expenses | $8 | $32 |
| Distribution costs | 8 | 14 |
| Marketing costs, excluding credit card operations | 3 | (5) |
| Corporate expenses | (11) | 5 |
| Net revenues from credit card operations | (12) | (30) |
| (Decrease)/Increase in SG&A | $(4) | $16 |

Many of our expenses, including store payroll and distribution costs, are variable in nature. These costs generally increase as sales increase and decrease as sales decrease. We measure both the change in these variable expenses and the expense as a percent of sales. If the expense as a percent of sales decreased from the prior year, the expense "leveraged" and indicates that the expense was well-managed or effectively generated additional sales. If the expense as a percent of sales increased over the prior year, the expense "deleveraged" and indicates that sales growth was less than expense growth. SG&A as a percent of sales increased, or "deleveraged," by approximately 15 basis points for the quarter and 10 basis points year to date.

The increases in store expenses are the result of higher store payroll, higher rent-related expenses due to new stores, and higher controllable expenses including repairs and maintenance. The timing and number of remodels resulted in higher expenses for the quarter and lower expenses year to date.

Marketing costs deleveraged for the quarter as we increased our spending in digital and broadcast and added California and Pittsburgh to our loyalty program pilot. Year to date, advertising leveraged approximately 5 basis points.

IT spending, which is included in corporate expenses, increased over both prior year periods due to growth and infrastructure investments related to our omni-channel strategy. For the quarter, these increases were more than offset by lower payroll and benefit expenses, including incentive compensation. Year to date, the IT spending increases were only partially offset by lower payroll and benefit expenses.

Distribution costs deleveraged in both the quarter and year to date due to higher distribution and fulfillment costs related to our growing E-Commerce business.

The increases in net revenues from credit card operations are the result of higher finance charge revenues and late fees due to growth in the portfolio. Partially offsetting these increases were higher bad debt expenses and operational costs. Year-to-date expenses are also higher as a result of the new credit card servicing platform which was implemented in the first quarter of 2012.

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Other Expenses.

| | Quarter | | Increase (Decrease) | | Year to Date | | Increase (Decrease) | |
|---|---|---|---|---|---|---|---|---|
| | 2013 | 2012 | $ | % | 2013 | 2012 | $ | % |
| | (Dollars in Millions) | | | | | | | |
| Depreciation and amortization | $228 | $210 | $18 | 9 % | $665 | $620 | $45 | 7 % |
| Interest expense, net | 84 | 80 | 4 | 5 | 251 | 243 | 8 | 3 |
| Provision for income taxes | 104 | 130 | (26) | (20) | 327 | 351 | (24) | (7) |
| Effective tax rate | 37.0 % | 37.8 % | | | 37.0 % | 36.6 % | | |

The increases in depreciation and amortization are primarily due to technology investments across the Company. The increases in interest expense are primarily due to the September 2012 and 2013 debt issuances. The decrease in the effective tax rate for the quarter was primarily due to tax credits which were identified during the quarter. The increase in the effective tax rate for the year was due to favorable settlements of state tax audits in 2012.

Seasonality and Inflation

Our business, like that of most retailers, is subject to seasonal influences, with the major portion of sales and income typically realized during the second half of each fiscal year, which includes the back-to-school and holiday seasons. Approximately 15% of annual sales typically occur during the back-to-school season and 30% during the holiday season. Because of the seasonality of our business, results for any quarter are not necessarily indicative of the results that may be achieved for a full fiscal year. Revenues and expenses associated with the opening of new stores may also effect our quarterly results.

Although we expect that our operations will be influenced by general economic conditions, including rising food, fuel and energy prices, we do not believe that inflation has had a material effect on our results of operations. However, there can be no assurance that our business will not be affected by such factors in the future. In 2012, we saw modest increases in apparel costs in the first six months and mid-single-digit decreases in the last six months of the year. In 2013, we have seen decreases in apparel costs.

Financial Condition and Liquidity

Our primary ongoing cash requirements are for capital expenditures for new stores, remodels and IT spending and for seasonal and new store inventory purchases. Share repurchases and dividend payments to shareholders are currently other significant usages of cash. These payments are discretionary and can be discontinued at any time should we require cash for other uses. Our primary sources of funds are cash flows provided by operations, short-term trade credit and our lines of credit. Short-term trade credit, in the form of extended payment terms for inventory purchases, often represents a significant source of financing for merchandise inventories. We may from time to time issue new debt. The amount of new debt issued, if any, will depend on prevailing market conditions, our cash needs and our capital structure. Seasonal cash needs may be met by cash on hand and/or the line of credit available under our revolving credit facility. Our working capital and inventory levels typically build throughout the fall, peaking during the November and December holiday selling season.

| | | | Increase in Cash | |
|---|---|---|---|---|
| | 2013 | 2012 | $ | % |
| Net cash provided by (used in): | (Dollars in Millions) | | | |
| Operating activities | $1,014 | $703 | $311 | 44 % |
| Investing activities | (451) | (568) | 117 | 21 % |
| Financing activities | (502) | (790) | 288 | 36 % |

Operating Activities. Operating activities generated $1.0 billion of cash in 2013, compared to $703 million in 2012. Merchandise inventory, excluding E-Commerce, decreased 1% from October 27, 2012 as inventory returned to more normalized levels in 2013. Due to the 53rd week in 2012, our inventory levels at the end of the current quarter more closely align with those from our first week of the fourth quarter of 2012. On this shifted basis, merchandise inventory dollars per store, excluding E-Commerce, decreased 5%.

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Accounts payable as a percent of inventory was 45.6% at November 2, 2013, compared to 50.1% at October 27, 2012. The decrease is primarily due to reducing our third quarter inventory receipts to manage our inventory levels as well as slower inventory turn.

Investing Activities. Net cash used in investing activities reflects a $176 million decrease in capital spending primarily due to fewer remodels and new stores as well as lower spending on E-Commerce fulfillment centers, partially offset by higher technology spending. We currently expect capital expenditures of approximately $725 million for fiscal 2013.

Financing Activities. Financing activities used cash of $502 million in 2013 and $790 million in 2012.

We paid cash for treasury stock purchases of $562 million in 2013 and $883 million in 2012. Share repurchases are discretionary in nature. The timing and amount of repurchases is based upon available cash balances, our stock price and other factors.

We paid cash dividends of $229 million ($1.05 per share) in 2013 and $227 million ($0.96 per share) in 2012. On November 13, 2013, our board of directors declared a quarterly cash dividend of $0.35 per common share. The dividend is payable December 24, 2013 to shareholders of record at the close of business on December 11, 2013.

In September 2013, we issued $300 million of 4.75% notes with semi-annual interest payments beginning in December 2013. In September 2012, we issued $350 million of 3.25% notes with semi-annual interest payments beginning in February 2013.

Free Cash Flow. We generated $480 million more in free cash flow in the first nine months of 2013 than in the first nine months of 2012. The increase is primarily due to higher cash from operating activities and lower capital expenditures, as discussed in more detail above. Free cash flow is a non-GAAP financial measure which we define as net cash provided by operating activities and proceeds from financing obligations (which generally represent landlord reimbursements of construction costs) less capital expenditures and capital lease and financing obligations. Free cash flow should be evaluated in addition to, and not considered a substitute for, other financial measures such as net income and cash flow provided by operations. We believe that free cash flow represents our ability to generate excess cash flow from our business operations.

The following table reconciles net cash provided by operating activities (a GAAP measure) to free cash flow (a non-GAAP measure).

| | 2013 | 2012 | Increase (Decrease) |
|---|---|---|---|
| | (In Millions) | | |
| Net cash provided by operating activities | $1,014 | $703 | $311 |
| Acquisition of property & equipment | (465) | (641) | 176 |
| Capital lease & financing obligation payments | (87) | (87) | — |
| Proceeds from financing obligations | — | 7 | (7) |
| Free cash flow | $462 | $(18) | $480 |

Key financial ratios. Key financial ratios that provide certain measures of our liquidity are as follows:

| | November 2, 2013 | October 27, 2012 |
|---|---|---|
| Liquidity Ratios: | | |
| Working capital (In Millions) | $2,346 | $2,102 |
| Current ratio | 1.64 | 1.57 |
| Debt/capitalization | 45.2% | 42.9% |

The increases in working capital and the current ratio as of November 2, 2013 compared to October 27, 2012 are due to higher cash and inventory levels and lower accounts payable, partially offset by leases and other accrued liabilities. The increase in the debt/capitalization ratio reflects the issuance of $300 million of debt in September 2013 and lower capitalization, primarily due to share repurchases.

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Debt Covenant Compliance. As of November 2, 2013, we were in compliance with all debt covenants and expect to remain in compliance during fiscal 2013.

| | (Dollars in Millions) |
|---|---|
| Included Indebtedness | |
| Total debt | $ 4,891 |
| Permitted exclusions | (8 ) |
| Subtotal | 4,883 |
| Rent x 8 | 2,136 |
| Included Indebtedness | $ 7,019 |
| Rolling 12-month EBITDAR | |
| Net income | $ 933 |
| Rent expense | 267 |
| Depreciation and amortization | 879 |
| Net interest | 336 |
| Provision for income taxes | 550 |
| Stock based compensation | 55 |
| Other non-cash revenues and expenses | 14 |
| Rolling 12-month EBITDAR | $ 3,034 |
| Debt Ratio (a) | 2.31 |
| Maximum permitted Debt Ratio | 3.75 |

(a) Included Indebtedness divided by Rolling 12-month EBITDAR

Contractual Obligations

Other than the $300 million of debt issued in September 2013, there have been no significant changes in the contractual obligations disclosed in our 2012 Form 10-K.

Off-Balance Sheet Arrangements

We have not provided any financial guarantees as of November 2, 2013. We have not created, and are not party to, any special-purpose or off-balance sheet entities for the purpose of raising capital, incurring debt or operating our business. We do not have any arrangements or relationships with entities that are not consolidated into our financial statements that are reasonably likely to materially affect our liquidity or the availability of capital resources.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires us to make estimates and assumptions that affect reported amounts. Management has discussed the development, selection and disclosure of its estimates and assumptions with the Audit Committee of our Board of Directors. There have been no significant changes in the critical accounting policies and estimates discussed in our 2012 Form 10-K.

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

There have been no significant changes in the market risks described in our 2012 Form 10-K.

## Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (the “Evaluation”) at a reasonable assurance level as of the last day of the period covered by this Report.

Based upon the Evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective at the reasonable assurance level. Disclosure controls and procedures are defined by Rules

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13a-15(e) of the Securities Exchange Act of 1934 (the "Exchange Act") as controls and other procedures that are designed to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures.

It should be noted that the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving our stated goals under all potential future conditions, regardless of how remote.

(b) Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended November 2, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

### Item 1A. Risk Factors

There have been no significant changes in our risk factors from those described in our 2012 Form 10-K.

Forward-looking Statements

This report contains statements that may constitute forward-looking statements within the meaning of the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. Those statements relate to developments, results, conditions or other events we expect or anticipate will occur in the future. Words such as “believes,” “anticipates,” “plans,” “expects” and similar expressions are intended to identify forward-looking statements. Without limiting the foregoing, these statements may relate to future outlook, revenues, earnings, store openings, planned capital expenditures, market conditions, new strategies and the competitive environment. Forward-looking statements are based on our management’s then current views and assumptions and, as a result, are subject to certain risks and uncertainties that could cause actual results to differ materially from those projected. Any such forward-looking statements are qualified by the important risk factors, described in Item 1A of our 2012 Form 10-K, that could cause actual results to differ materially from those predicted by the forward-looking statements. Forward-looking statements relate to the date initially made, and we undertake no obligation to update them. An investment in our common stock or other securities carries certain risks. Investors should carefully consider the risks as stated in our 2012 Form 10-K and other risks which may be disclosed from time to time in our filings with the SEC before investing in our securities.

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

We did not sell any securities during the quarter ended November 2, 2013 which were not registered under the Securities Act.

The following table contains information for shares repurchased and shares acquired from employees in lieu of amounts required to satisfy minimum tax withholding requirements upon the vesting of the employees’ restricted stock during the three fiscal months ended November 2, 2013:

| Period | Total Number of Shares Purchased | Average Price Paid Per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs |
|---|---|---|---|---|
| | | | | (In Millions) |

| | | | | |
|---|---|---|---|---|
| August 4 – August 31, 2013 | 1,972,883 | $51.22 | 1,972,139 | $ 2,743 |
| September 1 – October 5, 2013 | 2,109,467 | 52.01 | 2,102,172 | 2,634 |
| October 6 – November 2, 2013 | 1,189,408 | 52.65 | 1,176,233 | 2,572 |
| Total | 5,271,758 | $51.86 | 5,250,544 | $ 2,572 |

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Item 6. Exhibits

| Exhibit Number | Description |
|---|---|
| 4.1 | Seventh Supplemental Indenture dated September 12, 2013 between the Company and The Bank of New York Mellon Trust Company, N.A., formerly known as The Bank of New York Trust Company, N.A., as successor to The Bank of New York, as Trustee, incorporated by reference to Exhibit 4.1 of the Company's Current Report on Form 8-K dated September 5, 2013. |
| 4.2 | Form of $300,000,000 4.750% Notes due 2023, incorporated by reference to Exhibit 4.2 of the Company's Current Report on Form 8-K dated September 5, 2013. |
| 31.1 | Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase |

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Kohl’s Corporation
(Registrant)

Date: December 6, 2013

/s/ Wesley S. McDonald
Wesley S. McDonald
On behalf of the Registrant and as Senior Executive Vice President and Chief Financial Officer

(Principal Financial and Chief Accounting Officer)