

NORDSTROM INC
Form 10-Q
August 30, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
(Mark One)

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

For the quarterly period ended July 30, 2016

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: 001-15059

NORDSTROM, INC.

(Exact name of registrant as specified in its charter)

Washington 91-0515058
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

1617 Sixth Avenue, Seattle, Washington 98101
(Address of principal executive offices) (Zip Code)
206-628-2111

(Registrant's telephone number, including area code)

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 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 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.

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES NO

Common stock outstanding as of August 24, 2016: 173,440,084 shares

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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited).

NORDSTROM, INC.

CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS

(Amounts in millions except per share amounts)

(Unaudited)

| | Quarter Ended | | Six Months Ended | |
|--|------------------|-------------------|------------------|-------------------|
| | July 30, 2016 | August 1, 2015 | July 30, 2016 | August 1, 2015 |
| Net sales | \$3,592 | \$3,598 | \$6,784 | \$6,714 |
| Credit card revenues, net | 59 | 103 | 116 | 202 |
| Total revenues | 3,651 | 3,701 | 6,900 | 6,916 |
| Cost of sales and related buying and occupancy costs | (2,359) | (2,327) | (4,459) | (4,326) |
| Selling, general and administrative expenses | (1,071) | (997) | (2,114) | (1,968) |
| Earnings before interest and income taxes | 221 | 377 | 327 | 622 |
| Interest expense, net | (30) | (32) | (61) | (65) |
| Earnings before income taxes | 191 | 345 | 266 | 557 |
| Income tax expense | (74) | (134) | (103) | (218) |
| Net earnings | \$117 | \$211 | \$163 | \$339 |
| Earnings per share: | | | | |
| Basic | \$0.67 | \$1.11 | \$0.94 | \$1.78 |
| Diluted | \$0.67 | \$1.09 | \$0.93 | \$1.74 |

Weighted-average shares outstanding:

| | | | | |
|---------|-------|-------|-------|-------|
| Basic | 173.5 | 189.4 | 173.3 | 190.0 |
| Diluted | 174.8 | 193.5 | 175.2 | 194.2 |

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

NORDSTROM, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE EARNINGS

(Amounts in millions)

(Unaudited)

| | Quarter Ended | | Six Months Ended | |
|---|------------------|-------------------|------------------|-------------------|
| | July 30, 2016 | August 1, 2015 | July 30, 2016 | August 1, 2015 |
| Net earnings | \$117 | \$211 | \$163 | \$339 |
| Postretirement plan adjustments, net of tax | — | 1 | 1 | 3 |
| Foreign currency translation adjustment | (10) | (10) | 17 | (5) |
| Comprehensive net earnings | \$107 | \$202 | \$181 | \$337 |

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

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NORDSTROM, INC.
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (Amounts in millions)
 (Unaudited)

| | July 30, 2016 | January 30, 2016 | August 1, 2015 |
|---|------------------|---------------------|-------------------|
| Assets | | | |
| Current assets: | | | |
| Cash and cash equivalents | \$892 | \$595 | \$423 |
| Accounts receivable held for sale | — | — | 2,391 |
| Accounts receivable, net | 263 | 196 | 241 |
| Merchandise inventories | 2,032 | 1,945 | 2,004 |
| Current deferred tax assets, net | — | — | 256 |
| Prepaid expenses and other | 163 | 278 | 117 |
| Total current assets | 3,350 | 3,014 | 5,432 |
| Land, property and equipment (net of accumulated depreciation of \$5,330, \$5,108 and \$4,912) | 3,812 | 3,735 | 3,570 |
| Goodwill | 435 | 435 | 447 |
| Other assets | 533 | 514 | 251 |
| Total assets | \$8,130 | \$7,698 | \$9,700 |
| Liabilities and Shareholders' Equity | | | |
| Current liabilities: | | | |
| Accounts payable | \$1,604 | \$1,324 | \$1,589 |
| Accrued salaries, wages and related benefits | 381 | 416 | 389 |
| Other current liabilities | 1,326 | 1,161 | 1,145 |
| Current portion of long-term debt | 10 | 10 | 333 |
| Total current liabilities | 3,321 | 2,911 | 3,456 |
| Long-term debt, net | 2,772 | 2,795 | 2,808 |
| Deferred property incentives, net | 530 | 540 | 560 |
| Other liabilities | 570 | 581 | 385 |
| Commitments and contingencies (Note 6) | | | |
| Shareholders' equity: | | | |
| Common stock, no par value: 1,000 shares authorized; 173.3, 173.5 and 188.2 shares issued and outstanding | 2,612 | 2,539 | 2,460 |
| (Accumulated deficit) Retained earnings | (1,635) | (1,610) |) 97 |
| Accumulated other comprehensive loss | (40) |) (58) |) (66) |
| Total shareholders' equity | 937 | 871 | 2,491 |
| Total liabilities and shareholders' equity | \$8,130 | \$7,698 | \$9,700 |

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

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NORDSTROM, INC.

CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(Amounts in millions except per share amounts)

(Unaudited)

| | Common Stock | | Accumulated | Accumulated | |
|---|--------------|---------|-------------|-------------|---------------|
| | Shares | Amount | Deficit | Other | Comprehensive |
| | | | | Loss | Total |
| Balance at January 30, 2016 | 173.5 | \$2,539 | (\$1,610) | (\$58) | \$871 |
| Net earnings | — | — | 163 | — | 163 |
| Other comprehensive earnings | — | — | — | 18 | 18 |
| Dividends (\$0.74 per share) | — | — | (128) | — | (128) |
| Issuance of common stock under stock compensation plans | 0.9 | 31 | — | — | 31 |
| Stock-based compensation | 0.2 | 42 | — | — | 42 |
| Repurchase of common stock | (1.3) | — | (60) | — | (60) |
| Balance at July 30, 2016 | 173.3 | \$2,612 | (\$1,635) | (\$40) | \$937 |

| | Common Stock | | Retained | Accumulated | |
|---|--------------|---------|----------|-------------|---------------|
| | Shares | Amount | Earnings | Other | Comprehensive |
| | | | | Loss | Total |
| Balance at January 31, 2015 | 190.1 | \$2,338 | \$166 | (\$64) | \$2,440 |
| Net earnings | — | — | 339 | — | 339 |
| Other comprehensive loss | — | — | — | (2) | (2) |
| Dividends (\$0.74 per share) | — | — | (142) | — | (142) |
| Issuance of common stock under stock compensation plans | 1.5 | 84 | — | — | 84 |
| Stock-based compensation | 0.1 | 38 | — | — | 38 |
| Repurchase of common stock | (3.5) | — | (266) | — | (266) |
| Balance at August 1, 2015 | 188.2 | \$2,460 | \$97 | (\$66) | \$2,491 |

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

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NORDSTROM, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in millions)

(Unaudited)

| | Six Months Ended | |
|---|---------------------|-------------------|
| | July 30, 2016 | August 1, 2015 |
| Operating Activities | | |
| Net earnings | \$163 | \$339 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | |
| Depreciation and amortization expenses | 319 | 277 |
| Amortization of deferred property incentives and other, net | (34) | (95) |
| Deferred income taxes, net | (53) | (24) |
| Stock-based compensation expense | 47 | 41 |
| Tax (deficiency) benefit from stock-based compensation | (1) | 13 |
| Excess tax benefit from stock-based compensation | (1) | (13) |
| Bad debt expense | — | 20 |
| Change in operating assets and liabilities: | | |
| Accounts receivable | (66) | (216) |
| Merchandise inventories | (59) | (280) |
| Prepaid expenses and other assets | 96 | (19) |
| Accounts payable | 262 | 240 |
| Accrued salaries, wages and related benefits | (40) | (30) |
| Other current liabilities | 175 | 56 |
| Deferred property incentives | 31 | 97 |
| Other liabilities | 12 | 9 |
| Net cash provided by operating activities | 851 | 415 |
| Investing Activities | | |
| Capital expenditures | (407) | (521) |
| Change in credit card receivables originated at third parties | — | (64) |
| Other, net | 33 | 4 |
| Net cash used in investing activities | (374) | (581) |
| Financing Activities | | |
| Proceeds from long-term borrowings, net of discounts | — | 16 |
| Principal payments on long-term borrowings | (5) | (4) |
| (Decrease) increase in cash book overdrafts | (18) | 49 |
| Cash dividends paid | (128) | (142) |
| Payments for repurchase of common stock | (59) | (267) |
| Proceeds from issuances under stock compensation plans | 30 | 71 |
| Excess tax benefit from stock-based compensation | 1 | 13 |
| Other, net | (1) | 26 |
| Net cash used in financing activities | (180) | (238) |

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| | | | |
|--|-------|-------|---|
| Net increase (decrease) in cash and cash equivalents | 297 | (404 |) |
| Cash and cash equivalents at beginning of period | 595 | 827 | |
| Cash and cash equivalents at end of period | \$892 | \$423 | |

Supplemental Cash Flow Information

| | | | |
|---------------------------------------|--------|-------|--|
| Cash paid during the period for: | | | |
| Income taxes (refund), net | (\$50) | \$209 | |
| Interest, net of capitalized interest | 67 | 70 | |

Non-cash investing and financing activities:

| | | | |
|--|---|-------|--|
| Accounts receivable reclassified from held for investment to held for sale | — | 2,391 | |
|--|---|-------|--|

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

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NORDSTROM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollar and share amounts in millions except per share, per option and per unit amounts)

(Unaudited)

NOTE 1: BASIS OF PRESENTATION

The accompanying Condensed Consolidated Financial Statements include the balances of Nordstrom, Inc. and its subsidiaries (the “Company”). All intercompany transactions and balances are eliminated in consolidation. The interim Condensed Consolidated Financial Statements have been prepared on a basis consistent in all material respects with the accounting policies described and applied in our 2015 Annual Report on Form 10-K (“Annual Report”), and reflect all adjustments of a normal recurring nature that are, in management’s opinion, necessary for the fair presentation of the results of operations, financial position and cash flows for the periods presented.

The Condensed Consolidated Financial Statements as of and for the periods ended July 30, 2016 and August 1, 2015 are unaudited. The Condensed Consolidated Balance Sheet as of January 30, 2016 has been derived from the audited Consolidated Financial Statements included in our 2015 Annual Report. The interim Condensed Consolidated Financial Statements should be read together with the Consolidated Financial Statements and related footnote disclosures contained in our 2015 Annual Report.

The preparation of our financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and disclosure of contingent assets and liabilities. We base our estimates on historical experience and other assumptions that we believe to be reasonable under the circumstances. Actual results may differ from these estimates and assumptions.

Our business, like that of other retailers, is subject to seasonal fluctuations. Due to our Anniversary Sale in July and the holidays in the fourth quarter, our sales are typically higher in the second and fourth quarters than in the first and third quarters of the fiscal year. In 2016, the Anniversary Sale event started one week later in July relative to last year, shifting one week of the event into the third quarter. Results for any quarter are not necessarily indicative of the results that may be achieved for a full fiscal year.

Loyalty Program

Prior to the second quarter of 2016, customers who used Nordstrom Visa or Nordstrom credit or debit cards were able to participate in the Nordstrom Rewards program. During the second quarter of 2016, the Nordstrom Rewards program was expanded to enable all customers to earn benefits regardless of how they choose to pay. Customers accumulate points based on their level of spending. Upon reaching a certain points threshold, customers receive Nordstrom Notes, which can be redeemed for any goods or services offered at Nordstrom full-line stores, Nordstrom.com, Nordstrom Rack and Nordstromrack.com/HauteLook. Customers who use Nordstrom private label credit or debit cards or Nordstrom Visa credit cards receive additional benefits, including reimbursements for alterations, shopping and fashion events and early access to the Anniversary Sale.

We estimate the net cost of Nordstrom Notes that will be issued and redeemed and record this cost as rewards points are accumulated. These costs, as well as reimbursed alterations, are recorded in cost of sales as we provide customers with products and services for these rewards. Other benefits of the loyalty program, including shopping and fashion events, are recorded in selling, general and administrative expenses.

Reclassification

Reclassifications were made to our fiscal 2015 Condensed Consolidated Statements of Earnings and Condensed Consolidated Statement of Cash Flows to conform with current period presentation.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2014-09, Revenue from Contracts with Customers, which was subsequently modified in August 2015 by ASU No. 2015-14, Revenue from Contracts with Customers: Deferral of the Effective Date. The core principle of ASU No. 2014-09 is that companies should recognize revenue when the transfer of promised goods or services to customers occurs in an amount that reflects what the company expects to receive. It requires additional disclosures to describe the nature, amount, timing and uncertainty of revenue and cash flows from contracts with customers. In early 2016,

the FASB issued additional ASUs which clarify the implementation guidance on principal versus agent considerations, on identifying performance obligations and licensing and on the revenue recognition criteria. This guidance is effective for us beginning in the first quarter of 2018. We are currently evaluating the impact these provisions will have on our Consolidated Financial Statements.

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NORDSTROM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollar and share amounts in millions except per share, per option and per unit amounts)

(Unaudited)

In February 2016, the FASB issued ASU No. 2016-02, Leases. This ASU increases transparency and comparability by recognizing a lessee's rights and obligations resulting from leases by recording them on the balance sheet as lease assets and lease liabilities. The new standard requires lessees to apply a dual approach, classifying leases as either finance or operating leases based on the principle of whether or not the lease is effectively a financed purchase by the lessee. This classification dictates whether lease expense is to be recognized based on an effective interest method or on a straight-line basis over the term of the lease. This ASU is effective for us beginning with the first quarter of 2019. Though we are currently evaluating the impact of these provisions, we expect it will have a material impact on our Consolidated Financial Statements.

In March 2016, the FASB issued ASU 2016-09, Compensation — Stock Compensation — Improvements to Employee Share-Based Payment Accounting. This ASU impacts several aspects of the accounting for share-based payment transactions, including income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. This ASU is effective for us beginning with the first quarter of 2017. We are currently evaluating the impact these provisions will have on our Consolidated Financial Statements.

NOTE 2: CREDIT CARD RECEIVABLE TRANSACTION

On October 1, 2015, we completed the sale of a substantial majority of our U.S. Visa and private label credit card portfolio to TD Bank, N.A. ("TD") and we entered into a long-term program agreement under which TD is the exclusive issuer of our U.S. consumer credit cards.

In connection with the close of the credit card receivable transaction, we completed the defeasance of our \$325 Series 2011-1 Class A Notes in order to provide the credit card receivables to TD free and clear. At close, we received \$2.2 billion in cash consideration reflecting the par value of the receivables sold and incurred \$32 in transaction-related expenses during the third quarter of 2015. Pursuant to the agreement, we are obligated to offer and administer our loyalty program and perform other account servicing functions. In return, we receive a portion of the ongoing credit card revenue, net of credit losses, from both the sold and newly generated credit card receivables.

We recorded certain assets and liabilities associated with the arrangement. The beneficial interest asset is carried at fair value (see Note 5: Fair Value Measurements) and is amortized over approximately four years based primarily on the payment rate of the associated receivables. The deferred revenue and investment in contract asset are recognized/amortized over seven years on a straight line basis, following the delivery of the contract obligations and expected life of the agreement. We record each of these items in credit card revenue, net in our Condensed Consolidated Statements of Earnings.

NOTE 3: ACCOUNTS RECEIVABLE

The components of accounts receivable are as follows:

| | July 30, January 30, August 1, | | |
|--|--------------------------------|-------|-------|
| | 2016 | 2016 | 2015 |
| Credit card receivables and other, net | \$264 | \$197 | \$242 |
| Allowance for credit losses | (1) | (1) | (1) |
| Accounts receivable, net | \$263 | \$196 | \$241 |

Accounts receivable held for sale \$— \$— \$2,391

Credit card receivables and other, net primarily consist of employee credit card receivables and receivables from non-Nordstrom-branded cards.

In connection with our May 2015 purchase and sale agreement with TD, the accounts receivable discussed in Note 2: Credit Card Receivable Transaction, were recorded at the lower of cost (par) or fair value and reclassified as "held for sale." This resulted in the recognition of a \$64 benefit in the second quarter of 2015, due to the reversal of the allowance for credit losses. We subsequently sold the receivables to TD on October 1, 2015. There have been no

material changes to the delinquency status or net credit losses of the receivables sold.

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NORDSTROM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollar and share amounts in millions except per share, per option and per unit amounts)

(Unaudited)

NOTE 4: DEBT AND CREDIT FACILITIES

Debt

A summary of our long-term debt, including capital leases, is as follows:

| | July 30, 2016 | January 30, 2016 | August 1, 2015 |
|--|------------------|---------------------|-------------------|
| Secured | | | |
| Series 2011-1 Class A Notes, 2.28%, due October 2016 | \$— | \$— | \$325 |
| Mortgage payable, 7.68%, due April 2020 | 27 | 30 | 33 |
| Other | 4 | 5 | 9 |
| Total secured debt | 31 | 35 | 367 |
| Unsecured | | | |
| Net of unamortized discount: | | | |
| Senior notes, 6.25%, due January 2018 | 649 | 649 | 649 |
| Senior notes, 4.75%, due May 2020 | 499 | 499 | 499 |
| Senior notes, 4.00%, due October 2021 | 500 | 500 | 499 |
| Senior debentures, 6.95%, due March 2028 | 300 | 300 | 300 |
| Senior notes, 7.00%, due January 2038 | 146 | 146 | 146 |
| Senior notes, 5.00%, due January 2044 | 601 | 600 | 599 |
| Other | 56 | 76 | 82 |
| Total unsecured debt | 2,751 | 2,770 | 2,774 |
| Total long-term debt | 2,782 | 2,805 | 3,141 |
| Less: current portion | (10) | (10) | (333) |
| Total due beyond one year | \$2,772 | \$2,795 | \$2,808 |

In the third quarter of 2015, as a condition of closing the credit card receivable transaction (see Note 2: Credit Card Receivable Transaction), we defeased \$325 in secured Series 2011-1 Class A Notes in order to provide the receivables to TD free and clear.

Credit Facilities

As of July 30, 2016, we had total short-term borrowing capacity of \$800 under our senior unsecured revolving credit facility (“revolver”) that expires in April 2020, with an option to extend for an additional year. Under the terms of our revolver, we pay a variable rate of interest and a commitment fee based on our debt rating. The revolver is available for working capital, capital expenditures and general corporate purposes. We have the option to increase the revolving commitment by up to \$200, to a total of \$1,000, provided that we obtain written consent from the lenders. As of July 30, 2016, we had no issuances outstanding under our commercial paper program and no borrowings outstanding under our revolver.

The revolver requires that we maintain an adjusted debt to earnings before interest, income taxes, depreciation, amortization and rent (“EBITDAR”) leverage ratio of less than four times. As of July 30, 2016, we were in compliance with this covenant.

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NORDSTROM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollar and share amounts in millions except per share, per option and per unit amounts)

(Unaudited)

NOTE 5: FAIR VALUE MEASUREMENTS

We disclose our financial assets and liabilities that are measured at fair value in our Condensed Consolidated Balance Sheets by level within the fair value hierarchy as defined by applicable accounting standards:

Level 1: Quoted market prices in active markets for identical assets or liabilities

Level 2: Other observable market-based inputs or unobservable inputs that are corroborated by market data

Level 3: Unobservable inputs that cannot be corroborated by market data that reflect the reporting entity's own assumptions

Financial Instruments Measured at Fair Value on a Recurring Basis

We recorded a beneficial interest asset when we completed the sale of a substantial majority of our U.S. Visa and private label credit card portfolio (see Note 2: Credit Card Receivable Transaction). We determined the fair value of the beneficial interest asset based on a discounted cash flow model using Level 3 inputs of the fair value hierarchy. Inputs and assumptions include the discount rate, payment rate, credit loss rate and revenues and expenses associated with the program agreement. Given our review of market participant capital structures in the banking and credit card industries and our historical and expected portfolio performance, we used the following ranges of input assumptions to determine the fair value as of July 30, 2016:

| | Minimum | Maximum | | |
|---|---------|---------|--|---|
| Discount rate | 12 | % 12 | | % |
| Monthly payment rate | 6 | % 11 | | % |
| Annual credit loss rate | 3 | % 4 | | % |
| Annual revenues as a percent to credit card receivables | 13 | % 18 | | % |
| Annual expenses as a percent to credit card receivables | 5 | % 9 | | % |

We recognized \$7 and \$17 of amortization expense for the quarter and six months ended July 30, 2016 on the beneficial interest asset, which had a fair value of \$20 and \$37 as of July 30, 2016 and January 30, 2016. Amortization primarily reflects payments received on the receivables sold and is recorded in credit card revenues, net.

We did not have any financial assets or liabilities that were measured at fair value on a recurring basis as of August 1, 2015.

Financial Instruments Measured at Fair Value on a Nonrecurring Basis

We did not have any financial assets or liabilities that were measured at fair value on a nonrecurring basis as of July 30, 2016 and January 30, 2016.

As of August 1, 2015, our U.S. Visa and private label credit card receivables were "held for sale" and were recorded at the lower of cost (par) or fair value. We estimated the fair value of our credit card receivables "held for sale" based on a discounted cash flow model using estimates and assumptions regarding future credit card portfolio performance. This fair value estimate was primarily based on Level 3 inputs in the fair value hierarchy, including the discount rate, payment rate, credit losses, revenues and expenses. The estimated fair value of our credit card receivables "held for sale" was approximately 3% above par. This premium was solely associated with our credit card receivables "held for sale," and did not encompass other terms and elements within our agreement with TD.

Financial Instruments Not Measured at Fair Value

Financial instruments not measured at fair value on a recurring basis include cash and cash equivalents, accounts receivable, accounts payable and certificates of deposit, which approximate fair value due to their short-term nature, and long-term debt.

We estimate the fair value of our long-term debt using quoted market prices of the same or similar issues and, as such, this is considered a Level 2 fair value measurement. The following table summarizes the carrying value and fair value estimate of our long-term debt, including current maturities:

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| | July 30, 2016 | January 30, 2016 | August 1, 2015 |
|----------------------------------|------------------|---------------------|-------------------|
| Carrying value of long-term debt | \$2,782 | \$2,805 | \$3,141 |
| Fair value of long-term debt | 3,076 | 3,077 | 3,526 |

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NORDSTROM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollar and share amounts in millions except per share, per option and per unit amounts)

(Unaudited)

Non-financial Assets Measured at Fair Value on a Nonrecurring Basis

We also measure certain non-financial assets at fair value on a nonrecurring basis, primarily goodwill, investment in contract asset and long-lived tangible and intangible assets, in connection with periodic evaluations for potential impairment. There were no material impairment charges for these assets for the six months ended July 30, 2016 and August 1, 2015. We estimate the fair value of these assets using primarily unobservable inputs and, as such, these are considered Level 3 fair value measurements.

NOTE 6: COMMITMENTS AND CONTINGENCIES

Plans for our Manhattan full-line store, which we currently expect to open in 2019, ultimately include owning a condominium interest in a mixed-use tower and leasing certain nearby properties. As of July 30, 2016, we had approximately \$201 of fee interest in land, which is expected to convert to a condominium interest once the store is constructed. We have committed to make future installment payments based on the developer meeting pre-established construction and development milestones. In the event that this project is not completed, the opening may be delayed and we may be subject to future losses or capital commitments in order to complete construction or to monetize our investment in the land.

NOTE 7: SHAREHOLDERS' EQUITY

On October 1, 2015, our Board of Directors authorized a program to repurchase up to \$1,000 of our outstanding common stock through March 1, 2017. During the six months ended July 30, 2016, we repurchased 1.3 shares of our common stock for an aggregate purchase price of \$60 and had \$751 remaining in share repurchase capacity as of July 30, 2016. The actual number, price, manner and timing of future share repurchases, if any, will be subject to market and economic conditions and applicable Securities and Exchange Commission ("SEC") rules.

In August 2016, subsequent to quarter end, we declared a quarterly dividend of \$0.37 per share, which will be paid on September 13, 2016.

NOTE 8: STOCK-BASED COMPENSATION

The following table summarizes our stock-based compensation expense:

| | Quarter Ended | | Six Months Ended | |
|---|---------------|----------------|------------------|----------------|
| | July 30, 2016 | August 1, 2015 | July 30, 2016 | August 1, 2015 |
| Stock options | \$11 | \$10 | \$19 | \$19 |
| Restricted stock units | 9 | 6 | 15 | 10 |
| Acquisition-related stock compensation | 4 | 4 | 8 | 9 |
| Performance share units | 1 | — | 1 | — |
| Other | 2 | 2 | 4 | 3 |
| Total stock-based compensation expense, before income tax benefit | 27 | 22 | 47 | 41 |
| Income tax benefit | (9) | (7) | (15) | (13) |
| Total stock-based compensation expense, net of income tax benefit | \$18 | \$15 | \$32 | \$28 |

The following table summarizes our grants:

| | Six Months Ended | | Six Months Ended | |
|------------------------|------------------|----------------|---|---|
| | July 30, 2016 | August 1, 2015 | July 30, 2016 | August 1, 2015 |
| | Granted | Granted | Weighted-average grant-date fair value per unit | Weighted-average grant-date fair value per unit |
| Stock options | 2.9 | 1.7 | \$15 | \$21 |
| Restricted stock units | 1.6 | 0.4 | \$43 | \$78 |

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NORDSTROM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollar and share amounts in millions except per share, per option and per unit amounts)

(Unaudited)

NOTE 9: EARNINGS PER SHARE

The computation of earnings per share is as follows:

| | Quarter Ended | | Six Months Ended | |
|--|---------------|----------------|------------------|----------------|
| | July 30, 2016 | August 1, 2015 | July 30, 2016 | August 1, 2015 |
| Net earnings | \$117 | \$211 | \$163 | \$339 |
| Basic shares | 173.5 | 189.4 | 173.3 | 190.0 |
| Dilutive effect of stock options and other | 1.3 | 4.1 | 1.9 | 4.2 |
| Diluted shares | 174.8 | 193.5 | 175.2 | 194.2 |
| Earnings per basic share | \$0.67 | \$1.11 | \$0.94 | \$1.78 |
| Earnings per diluted share | \$0.67 | \$1.09 | \$0.93 | \$1.74 |
| Anti-dilutive stock options and other | 13.6 | 1.7 | 10.2 | 1.7 |

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NORDSTROM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollar and share amounts in millions except per share, per option and per unit amounts)

(Unaudited)

NOTE 10: SEGMENT REPORTING

The following tables set forth information for our reportable segments:

| | Retail | Corporate/Other | Retail Business | Credit | Total |
|--|---------|-----------------|--------------------|---------|--------------|
| Quarter Ended July 30, 2016 | | | | | |
| Net sales | \$3,871 | (\$279 |) | \$3,592 | \$— \$3,592 |
| Credit card revenues, net | — | — |) | — | 59 59 |
| Earnings (loss) before interest and income taxes | 383 | (179 |) | 204 | 17 221 |
| Interest expense, net | — | (30 |) | (30 |) — (30) |
| Earnings (loss) before income taxes | 383 | (209 |) | 174 | 17 191 |
| Quarter Ended August 1, 2015 | | | | | |
| Net sales | \$3,775 | (\$177 |) | \$3,598 | \$— \$3,598 |
| Credit card revenues, net | — | — |) | — | 103 103 |
| Earnings (loss) before interest and income taxes | 378 | (115 |) | 263 | 114 377 |
| Interest expense, net | — | (27 |) | (27 |) (5) (32) |
| Earnings (loss) before income taxes | 378 | (142 |) | 236 | 109 345 |
| Six Months Ended July 30, 2016 | | | | | |
| Net sales | \$7,129 | (\$345 |) | \$6,784 | \$— \$6,784 |
| Credit card revenues, net | — | — |) | — | 116 116 |
| Earnings (loss) before interest and income taxes | 572 | (278 |) | 294 | 33 327 |
| Interest expense, net | — | (61 |) | (61 |) — (61) |
| Earnings (loss) before income taxes | 572 | (339 |) | 233 | 33 266 |
| Six Months Ended August 1, 2015 | | | | | |
| Net sales | \$6,966 | (\$252 |) | \$6,714 | \$— \$6,714 |
| Credit card revenues, net | — | — |) | — | 202 202 |
| Earnings (loss) before interest and income taxes | 658 | (197 |) | 461 | 161 622 |
| Interest expense, net | — | (55 |) | (55 |) (10) (65) |
| Earnings (loss) before income taxes | 658 | (252 |) | 406 | 151 557 |

Credit segment earnings before interest and income taxes for the quarter and six months ended August 1, 2015 included a \$64 benefit due to the reversal of the allowance for credit losses on accounts receivable that were reclassified to "held for sale" (see Note 3: Accounts Receivable).

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NORDSTROM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollar and share amounts in millions except per share, per option and per unit amounts)

(Unaudited)

The following table summarizes net sales within our reportable segments:

| | Quarter Ended | | Six Months Ended | |
|-----------------------------------|------------------|-------------------|------------------|-------------------|
| | July 30, 2016 | August 1, 2015 | July 30, 2016 | August 1, 2015 |
| Nordstrom full-line stores - U.S. | \$1,978 | \$2,097 | \$3,560 | \$3,796 |
| Nordstrom.com | 683 | 625 | 1,178 | 1,105 |
| Nordstrom | 2,661 | 2,722 | 4,738 | 4,901 |
| | | | | |
| Nordstrom Rack | 926 | 857 | 1,819 | 1,688 |
| Nordstromrack.com/HauteLook | 157 | 117 | 323 | 234 |
| Off-price | 1,083 | 974 | 2,142 | 1,922 |
| | | | | |
| Other retail ¹ | 127 | 79 | 249 | 143 |
| Total Retail segment | 3,871 | 3,775 | 7,129 | 6,966 |
| Corporate/Other | (279) | (177) | (345) | (252) |
| Total net sales | \$3,592 | \$3,598 | \$6,784 | \$6,714 |

¹ Other retail includes Nordstrom Canada full-line stores, Trunk Club and Jeffrey boutiques.

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

(Dollar and share amounts in millions except per share and per square foot amounts)

CAUTIONARY STATEMENT

Certain statements in this Quarterly Report on Form 10-Q contain or may suggest "forward-looking" information (as defined in the Private Securities Litigation Reform Act of 1995) that involve risks and uncertainties including, but not limited to, anticipated financial outlook for the fiscal year ending January 28, 2017, anticipated annual total and comparable sales rates, anticipated new store openings in existing, new and international markets, anticipated Return on Invested Capital and trends in our operations. Such statements are based upon the current beliefs and expectations of the Company's management and are subject to significant risks and uncertainties. Actual future results may differ materially from historical results or current expectations depending upon factors including, but not limited to:

Strategic and Operational

- successful execution of our customer strategy, including expansion into new domestic and international markets, acquisitions, investments in our stores and online as well as investments in technology, our ability to realize the anticipated benefits from growth initiatives and our ability to provide a seamless experience across all channels,
- timely and effective execution of our ecommerce initiatives and ability to manage the costs and organizational changes associated with this evolving business model,
- timely completion of construction associated with newly planned stores, relocations and remodels, all of which may be impacted by the financial health of third parties,
- our ability to maintain relationships with our employees and to effectively attract, develop and retain our future leaders,
- effective inventory management processes and systems, fulfillment processes and systems, disruptions in our supply chain and our ability to control costs,
- the impact of any systems failures, cybersecurity and/or security breaches, including any security breach of our systems or those of a third-party provider that results in the theft, transfer or unauthorized disclosure of customer, employee or Company information or compliance with information security and privacy laws and regulations in the event of such an incident,
- successful execution of our information technology strategy,
- our ability to effectively utilize data in strategic planning and decision making,
- efficient and proper allocation of our capital resources,
- our ability to realize the expected benefits, respond to potential risks and appropriately manage costs associated with our program agreement with TD,
- our ability to safeguard our reputation and maintain our vendor relationships,
- our ability to respond to the business environment, fashion trends and consumer preferences, including changing expectations of service and experience in stores and online, and evolve our business model,
- the effectiveness of planned advertising, marketing and promotional campaigns in the highly competitive retail industry,
- the timing, price, manner and amounts of share repurchases by the Company, if any, or any share issuances by the Company, including issuances associated with option exercises or other matters,

Economic and External

- the impact of economic and market conditions and the resultant impact on consumer spending patterns,
- weather conditions, natural disasters, health hazards, national security or other market disruptions, or the prospects of these events and the resulting impact on consumer spending patterns,

Legal and Regulatory

- our compliance with applicable domestic and international laws, regulations and ethical standards, including those related to banking, employment and tax and the outcome of claims and litigation and resolution of such matters,
- the impact of the current regulatory environment and financial system and health care reforms, and
- compliance with debt covenants, availability and cost of credit, changes in our credit rating, changes in interest rates, debt repayment patterns and personal bankruptcies.

These and other factors, including those factors described in Part I, “Item 1A. Risk Factors” in our 2015 Annual Report on Form 10-K could affect our financial results and cause actual results to differ materially from any forward-looking information we may provide. We undertake no obligation to update or revise any forward-looking statements to reflect subsequent events, new information or future circumstances.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.
(Continued) (Dollar and share amounts in millions except per share and per square foot amounts)

OVERVIEW

Our Anniversary Sale kicked off in July, which is our largest event of the year outside of the holiday season. We were pleased with the customer response to the event. This year marked one of the best events in our history, with an all-time high in sales volume. The strength of the Anniversary Sale, along with our inventory and expense execution, drove better than expected results for the second quarter.

Second quarter net earnings were \$117 compared with net earnings of \$211 during the same period in fiscal 2015 which included a \$64 benefit from a non-cash accounting adjustment. Our earnings per diluted share of \$0.67 exceeded expectations. We believe these results are reflective of our ongoing efforts to realign our resources and priorities to better serve customers.

Our Nordstrom Rewards program is one area that enables us to strengthen relationships with customers. It also serves as a powerful tool to drive incremental sales and trips. On May 18, we expanded the program so that all of our customers can earn rewards regardless of how they choose to pay. Based on the strong customer response, we now have approximately 6 million Nordstrom Rewards customers, up significantly from 4.7 million last quarter.

In continuing our efforts to improve our operating model, we recognize that the shift toward ecommerce is having an impact on our financial results. As we accelerated investments to support changes in customer expectations, our expenses -- particularly in supply chain, marketing and technology -- grew faster than sales. To address this, we are executing on several initiatives to enhance the customer experience and improve our operating performance:

In supply chain, we are optimizing our supplier network for both inbound and outbound carriers, reducing split shipments through a greater allocation of merchandise to our fulfillment centers and editing out less profitable items online. Since the opening of our East Coast fulfillment center last fall, our delivery times for customers we serve on the East Coast improved by more than 30% while reducing unit shipping costs due to the increased proximity to our customers.

In marketing, we are repositioning our organization to better align with the customer journey and our strategic priorities around customer acquisition and retention. This includes strengthening our capabilities around customer analytics and digital engagement so that we can reach customers in a more efficient and cost-effective manner.

In technology, we're on a path to modernize our platform and increase the productivity of delivering features that will improve the customer experience. We implemented a new technology solution that supports our expanded loyalty program, which enables us to better serve customers and increase their lifetime value.

Over the past several quarters, we have been actively addressing our inventory, expense and capital investments as we align with current sales trends. In the second quarter, we made substantial progress by bringing down inventory levels relative to sales. As we head into the second half of the year, we are focused on a number of initiatives to improve the customer experience and drive top-line growth:

We're expanding our reach to serve more customers. We're building on the success of our Canada expansion with two full-line store openings in Toronto in the third quarter. In the U.S., we plan to open a second full-line store in Austin, Texas and 15 Nordstrom Rack stores this fall.

Continuing our efforts to grow relevant brands that have limited distribution play an important role in creating excitement and attracting new customers. These brands now make up the majority of our top 20 fastest-growing vendors, and we're continuing to expand highly sought-after brands, like Ivy Park, Madewell and Charlotte Tilbury, with new partnerships to come.

We are making digital enhancements to better serve customers no matter how they choose to shop with us. We have several initiatives underway that include new mobile features, improvements to our website and enhanced selling tools. This fall we are piloting a mobile feature that gives customers the ability to reserve merchandise online and try on in our stores.

These efforts to improve our operations are expected to result in a more productive use of financial resources, which is beginning to positively impact our results. As our business evolves, we will continue to aggressively prioritize our resources to ensure that we can serve customers with high-quality products and services while achieving profitable growth. Through these ongoing efforts, we believe we will be well-positioned for future success.

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Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.
(Continued) (Dollar and share amounts in millions except per share and per square foot amounts)

RESULTS OF OPERATIONS

Our reportable segments are Retail and Credit. We analyze our results of operations through earnings before interest and income taxes for our Retail Business and Credit, while interest expense, income taxes, earnings per share and return on invested capital are discussed on a total Company basis.

Retail Business

Our Retail Business includes our Nordstrom U.S. and Canada full-line stores, Nordstrom.com, Nordstrom Rack stores, Nordstromrack.com/HauteLook, Trunk Club, Jeffrey and our Last Chance clearance store. For purposes of discussion and analysis of our results of operations of our Retail Business, we combine our Retail segment results with revenues and expenses in the “Corporate/Other” column of Note 10: Segment Reporting in Item 1 (collectively, the “Retail Business”).

Certain metrics we use to evaluate the Retail Business may not be calculated in a consistent manner among industry peers. Provided below are definitions of metrics we present within our analysis of the Retail Business:

- **Comparable Sales** – sales from stores that have been open at least one full year at the beginning of the year. Total Company comparable sales include sales from our online channels.
- **Gross Profit** – net sales less cost of sales and related buying and occupancy costs.
- **Inventory Turnover Rate** – annual cost of sales and related buying and occupancy costs (for all segments) divided by the trailing 4-quarter average inventory.
- **Total Sales Per Square Foot** – net sales divided by weighted-average square footage.
- **4-wall Sales Per Square Foot** – sales for Nordstrom U.S. and Canada full-line stores, Nordstrom Rack stores, Trunk Club clubhouses, Jeffrey boutiques and our Last Chance store divided by their weighted-average square footage.

Summary

The following table summarizes the results of our Retail Business:

| | Quarter Ended | | August 1, 2015 | |
|--|------------------|------------------------------------|------------------------------------|----------|
| | July 30, 2016 | Amount % of net sales ¹ | Amount % of net sales ¹ | % |
| Net sales | \$3,592 | 100.0 | % \$3,598 | 100.0 % |
| Cost of sales and related buying and occupancy costs | (2,358) | (65.6 | %) (2,326) | (64.6 %) |
| Gross profit | 1,234 | 34.4 | % 1,272 | 35.4 % |
| Selling, general and administrative expenses | (1,030) | (28.7 | %) (1,009) | (28.0 %) |
| Earnings before interest and income taxes | \$204 | 5.7 | % \$263 | 7.3 % |
| | Six Months Ended | | August 1, 2015 | |
| | July 30, 2016 | Amount % of net sales ¹ | Amount % of net sales ¹ | % |
| Net sales | \$6,784 | 100.0 | % \$6,714 | 100.0 % |
| Cost of sales and related buying and occupancy costs | (4,456) | (65.7 | %) (4,323) | (64.4 %) |
| Gross profit | 2,328 | 34.3 | % 2,391 | 35.6 % |
| Selling, general and administrative expenses | (2,034) | (30.0 | %) (1,930) | (28.7 %) |
| Earnings before interest and income taxes | \$294 | 4.3 | % \$461 | 6.9 % |

¹ Subtotals and totals may not foot due to rounding.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.
(Continued) (Dollar and share amounts in millions except per share and per square foot amounts)

Retail Business Net Sales

In our ongoing effort to enhance the customer experience, we are focused on providing customers with a seamless experience across our channels. While our customers may engage with us through multiple channels, we know they value the overall Nordstrom brand experience and view us simply as Nordstrom, which is ultimately how we view our business. To provide additional transparency into our net sales by channel, we present the following summary of our Retail Business:

| | Quarter Ended | | Six Months Ended | |
|--|------------------|-------------------|------------------|-------------------|
| | July 30, 2016 | August 1, 2015 | July 30, 2016 | August 1, 2015 |
| Net sales by channel: | | | | |
| Nordstrom full-line stores - U.S. | \$1,978 | \$2,097 | \$3,560 | \$3,796 |
| Nordstrom.com | 683 | 625 | 1,178 | 1,105 |
| Full-price | 2,661 | 2,722 | 4,738 | 4,901 |
| | | | | |
| Nordstrom Rack | 926 | 857 | 1,819 | 1,688 |
| Nordstromrack.com/HauteLook | 157 | 117 | 323 | 234 |
| Off-price | 1,083 | 974 | 2,142 | 1,922 |
| | | | | |
| Other retail ¹ | 127 | 79 | 249 | 143 |
| Retail segment | 3,871 | 3,775 | 7,129 | 6,966 |
| Corporate/Other | (279) | (177) | (345) | (252) |
| Total net sales | \$3,592 | \$3,598 | \$6,784 | \$6,714 |
| | | | | |
| Net sales (decrease) increase | (0.2 %) | 9.2 % | 1.0 % | 9.5 % |
| | | | | |
| Comparable sales increase (decrease) by channel: | | | | |
| Nordstrom full-line stores - U.S. | (6.5 %) | 0.8 % | (7.0 %) | 0.7 % |
| Nordstrom.com | 9.4 % | 20.4 % | 6.7 % | 20.1 % |
| Full-price | (2.8 %) | 4.8 % | (4.0 %) | 4.5 % |
| Nordstrom Rack | 1.1 % | 1.7 % | 0.2 % | 0.8 % |
| Nordstromrack.com/HauteLook | 34.7 % | 49.6 % | 38.3 % | 50.4 % |
| Off-price | 5.3 % | 6.5 % | 4.9 % | 5.7 % |
| Total Company | (1.2 %) | 4.9 % | (1.5 %) | 4.6 % |

Sales per square foot:

| | | | | |
|--|-------|-------|-------|-------|
| Total sales per square foot | \$125 | \$131 | \$236 | \$245 |
| 4-wall sales per square foot | 104 | 109 | 193 | 204 |
| Full-line sales per square foot - U.S. | 95 | 102 | 171 | 185 |
| Nordstrom Rack sales per square foot | 126 | 129 | 249 | 259 |

¹ Other retail includes Nordstrom Canada full-line stores, Trunk Club and Jeffrey boutiques.

Total Company net sales decreased 0.2% for the quarter and increased 1.0% for the six months ended July 30, 2016, compared with the same periods in 2015, while comparable sales decreased 1.2% for the quarter and 1.5% for the six months ended July 30, 2016. The Anniversary Sale, historically the largest event of the year, performed better than recent trends. This event started one week later in July relative to last year, shifting one week of the event into the third quarter. The shift had an unfavorable comparison to comparable sales of approximately 250 basis points in the second quarter.

To date in fiscal 2016, we relocated one full-line store and opened six Nordstrom Rack stores.

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(Continued) (Dollar and share amounts in millions except per share and per square foot amounts)

Full-price net sales, which consists of U.S. full-line and Nordstrom.com channels, decreased 2.2% for the quarter and 3.3% for the six months ended July 30, 2016, compared with the same periods in 2015, while on a comparable basis, sales decreased 2.8% and 4.0% for the quarter and six months ended July 30, 2016. Also on a comparable basis for the quarter and six months ended July 30, 2016, full-price experienced a decrease in the total number of items sold, partially offset by an increase in the average selling price per item sold. The top-performing merchandise categories were Beauty and Shoes for the quarter and six months ended July 30, 2016.

U.S. full-line stores' net sales decreased 5.7% and comparable sales decreased 6.5% for the quarter ended July 30, 2016, while for the six months ended July 30, 2016, net sales decreased 6.2% and comparable sales decreased 7.0%, compared with the same periods in 2015. Southern California was the top-performing geographic region for the quarter and six months ended July 30, 2016. Nordstrom.com net sales increased 9.4% for the quarter and 6.7% for the six months ended July 30, 2016.

Within our off-price offering, Nordstrom Rack net sales increased 8.0% and 7.8% for the quarter and six months ended July 30, 2016, compared with the same periods in 2015, attributable to 22 new store openings since the end of the second quarter of 2015. Nordstrom Rack comparable sales increased 1.1% for the quarter and 0.2% for the six months ended July 30, 2016. Also on a comparable basis for the quarter and six months ended July 30, 2016, the number of items sold increased at Nordstrom Rack, partially offset by a decrease in the average retail price. Handbags was the top-performing merchandise category and the East was the top-performing geographic region for the quarter and six months ended July 30, 2016.

Nordstromrack.com/HauteLook continued to experience outsized growth, as net sales increased 34.7% for the quarter and 38.3% for the six months ended July 30, 2016.

Retail Business Gross Profit

The following table summarizes the Retail Business gross profit ("Retail GP"):

| | Quarter Ended | | Six Months Ended | |
|---|---------------|-----------|------------------|-----------|
| | July 30, | August 1, | July 30, | August 1, |
| | 2016 | 2015 | 2016 | 2015 |
| Retail gross profit | \$1,234 | \$1,272 | \$2,328 | \$2,391 |
| Retail gross profit as a % of net sales | 34.4 % | 35.4 % | 34.3 % | 35.6 % |

| | July 30, | August 1, |
|----------------------------------|----------|-----------|
| | 2016 | 2015 |
| Ending inventory per square foot | \$70.51 | \$72.72 |
| Inventory turnover rate | 4.43 | 4.49 |

Our Retail GP rate decreased 100 basis points, or \$38 for the quarter and 130 basis points, or \$63 for the six months ended July 30, 2016 compared with the same periods in 2015. These decreases were primarily due to higher markdowns in addition to increased occupancy costs related to Nordstrom Rack's continued store expansion.

Through our actions to realign inventory levels and the performance of our Anniversary Sale, inventory growth slowed to 1.4% which drove improvement to our ending inventory per square foot.

Retail Business Selling, General and Administrative Expenses

Retail Business selling, general and administrative expenses ("Retail SG&A") are summarized in the following table:

| | Quarter Ended | | Six Months Ended | |
|---|---------------|-----------|------------------|-----------|
| | July 30, | August 1, | July 30, | August 1, |
| | 2016 | 2015 | 2016 | 2015 |
| Retail selling, general and administrative expenses | \$1,030 | \$1,009 | \$2,034 | \$1,930 |
| Retail selling, general and administrative expenses as a % of net sales | 28.7 % | 28.0 % | 30.0 % | 28.7 % |

For the quarter ended July 30, 2016, our Retail SG&A rate increased 64 basis points primarily attributable to expense deleverage from the shift in sales volume into the third quarter related to the Anniversary Sale event, while Retail SG&A expenses increased \$21 primarily due to increased technology investments. For the six months ended July 30,

2016, our Retail SG&A rate increased 123 basis points and our Retail SG&A increased \$104 primarily reflecting planned technology investments and higher credit chargeback expenses associated with an industry change in liability rules effective October 2015.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.
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Credit Segment

As we completed the sale of a substantial majority of our U.S. Visa and private label credit card portfolio to TD on October 1, 2015, and entered into a long-term program agreement under which TD is the exclusive issuer of our U.S. consumer credit cards, our Credit Segment business has changed. With these changes, although we receive a smaller share of available profits under the program agreement, we no longer fund this portfolio alleviating significant working capital requirements (see Note 2: Credit Card Receivable Transaction in Item 1).

Summary

The table below provides a detailed view of the operational results of our Credit segment, consistent with Note 10: Segment Reporting in Item 1:

| | Quarter Ended | | Six Months Ended | |
|---|---------------|----------------|------------------|----------------|
| | July 30, 2016 | August 1, 2015 | July 30, 2016 | August 1, 2015 |
| Credit card revenues, net | \$59 | \$103 | \$116 | \$202 |
| Credit expenses | (42) | (50) | (83) | (102) |
| Credit transaction, net | — | 61 | — | 61 |
| Earnings before interest and income taxes | 17 | 114 | 33 | 161 |
| Interest expense ¹ | — | (5) | — | (10) |
| Earnings before income taxes | \$17 | \$109 | \$33 | \$151 |

Credit and debit card volume²:

| | | | | |
|--------------|---------|---------|---------|---------|
| Outside | \$1,068 | \$1,097 | \$2,084 | \$2,150 |
| Inside | 1,708 | 1,730 | 2,975 | 2,999 |
| Total volume | \$2,776 | \$2,827 | \$5,059 | \$5,149 |

¹ Prior to the credit card receivable transaction, interest expense was allocated to the Credit segment as if it carried debt of up to 80% of the credit card receivables.

² Volume represents sales on the total portfolio plus applicable taxes.

Credit Card Revenues, net

The following is a summary of our credit card revenues, net:

| | Quarter Ended | | Six Months Ended | |
|---------------------------------|---------------|----------------|------------------|----------------|
| | July 30, 2016 | August 1, 2015 | July 30, 2016 | August 1, 2015 |
| Finance charge revenue | \$1 | \$64 | \$3 | \$128 |
| Interchange fees | 1 | 23 | 3 | 44 |
| Late fees and other | 1 | 16 | 1 | 30 |
| Credit program revenues, net | 56 | — | 109 | — |
| Total credit card revenues, net | \$59 | \$103 | \$116 | \$202 |

Prior to the close of the credit card receivable transaction on October 1, 2015, credit card revenues included finance charges, interchange fees, late fees and other revenue, recorded net of estimated uncollectible finance charges and fees. Finance charges represent interest earned on unpaid balances while interchange fees are earned from the use of Nordstrom Visa credit cards at merchants outside of Nordstrom. Late fees are assessed when a credit card account becomes past due. We continue to recognize revenue in this manner for the credit card receivables retained subsequent to the close of the credit card receivable transaction.

Following the close of the transaction and pursuant to the program agreement with TD, we receive our portion of the ongoing credit card revenue, net of credit losses, from both the sold and newly generated credit card receivables, which is recorded in credit program revenues, net. Revenue earned under the program agreement is impacted by the credit quality of receivables and factors such as deteriorating economic conditions, declining creditworthiness of

cardholders and the execution of account management and collection activities may heighten the risk of credit losses. Asset amortization and deferred revenue recognition associated with the assets and liabilities recorded as part of the transaction are also recognized in credit program revenues, net.

Credit card revenues, net decreased \$44 and \$86 for the quarter and six months ended July 30, 2016, compared with the same periods in 2015, primarily due to the impact of the program agreement with TD and the amortization of our beneficial interest asset.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.
(Continued) (Dollar and share amounts in millions except per share and per square foot amounts)

Credit Expenses

Credit expenses are summarized in the following table:

| | Quarter Ended | | Six Months Ended | |
|-----------------------|---------------|----------------|------------------|----------------|
| | July 30, 2016 | August 1, 2015 | July 30, 2016 | August 1, 2015 |
| Operational expenses | \$41 | \$39 | \$80 | \$79 |
| Bad debt expense | — | 10 | — | 20 |
| Occupancy expenses | 1 | 1 | 3 | 3 |
| Total credit expenses | \$42 | \$50 | \$83 | \$102 |

Total credit expenses decreased \$8 and \$19 for the quarter and six months ended July 30, 2016, compared with the same periods in 2015, primarily due to a decrease in bad debt expense since the sale of our credit card receivables in the third quarter of 2015.

Credit Transaction, net

Credit transaction, net of \$61 for the quarter and six months ended August 1, 2015 is primarily due to the reversal of the allowance for credit losses on accounts receivable that were reclassified to "held for sale" (see Note 3: Accounts Receivable).

Total Company Results

Interest Expense, net

Interest expense, net was \$30 for the second quarter and \$61 for the six months ended July 30, 2016, compared with \$32 for the second quarter and \$65 for the six months ended August 1, 2015. These decreases were primarily due to the defeasance of our \$325 Series 2011-1 Class A Notes in the third quarter of 2015 as a result of the credit card receivable transaction.

Income Tax Expense

Income tax expense is summarized in the following table:

| | Quarter Ended | | Six Months Ended | |
|--------------------|---------------|----------------|------------------|----------------|
| | July 30, 2016 | August 1, 2015 | July 30, 2016 | August 1, 2015 |
| Income tax expense | \$74 | \$134 | \$103 | \$218 |
| Effective tax rate | 38.7% | 38.9% | 38.7% | 39.2% |

The effective tax rate was relatively flat for the quarter ended July 30, 2016, compared with the same period in 2015. The effective tax rate decreased for the six months ended July 30, 2016, compared with the same period in 2015, primarily due to increased federal income tax credits.

Earnings Per Share

Earnings per share is as follows:

| | Quarter Ended | | Six Months Ended | |
|---------|---------------|----------------|------------------|----------------|
| | July 30, 2016 | August 1, 2015 | July 30, 2016 | August 1, 2015 |
| Basic | \$0.67 | \$1.11 | \$0.94 | \$1.78 |
| Diluted | \$0.67 | \$1.09 | \$0.93 | \$1.74 |

Earnings per diluted share decreased for the quarter and six months ended July 30, 2016, compared with the same periods in 2015, primarily due to a \$64 benefit in fiscal 2015 associated with the sale of the credit card portfolio and higher 2016 planned technology and fulfillment expenses supporting the Company's growth initiatives. This was partially offset by a decrease in weighted average shares outstanding resulting from increased share repurchases in the second half of 2015.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.
(Continued) (Dollar and share amounts in millions except per share and per square foot amounts)

2016 Outlook

We updated our annual earnings per diluted share expectations to incorporate our second quarter results. Our expectations for fiscal 2016 are as follows:

| | Prior Outlook | Current Outlook |
|---|--------------------------|----------------------------|
| Net sales (percent) | 2.5 to 4.5 increase | 2.5 to 4.5 increase |
| Comparable sales (percent) | 1 decrease to 1 increase | 1 decrease to 1 increase |
| Retail EBIT (percent) | 10 to 20 decrease | 10 to 15 decrease |
| Credit EBIT | \$70 to \$80 million | Approximately \$80 million |
| Earnings per diluted share (excluding the impact of any future share repurchases) | \$2.50 to \$2.70 | \$2.60 to \$2.75 |

Return on Invested Capital ("ROIC") (Non-GAAP financial measure)

We believe ROIC is a useful financial measure for investors in evaluating the efficiency and effectiveness of our use of capital and believe ROIC is an important component of shareholders' return over the long term. In addition, we incorporate ROIC in our executive incentive compensation measures. For the 12 fiscal months ended July 30, 2016, our ROIC decreased to 9.1% compared with 12.3% for the 12 fiscal months ended August 1, 2015, primarily due to reduced earnings.

We define ROIC as our net operating profit after tax divided by our average invested capital using the trailing 12-month average. ROIC is not a measure of financial performance under generally accepted accounting principles ("GAAP") and should be considered in addition to, and not as a substitute for, return on assets, net earnings, total assets or other financial measures prepared in accordance with GAAP. Our method of determining non-GAAP financial measures may differ from other companies' methods and therefore may not be comparable to those used by other companies. The financial measure calculated under GAAP which is most directly comparable to ROIC is return on assets. The following is a reconciliation of the components of ROIC and return on assets:

| | 12 Fiscal Months Ended | |
|--|------------------------|----------------|
| | July 30, 2016 | August 1, 2015 |
| Net earnings | \$424 | \$736 |
| Add: income tax expense | 261 | 481 |
| Add: interest expense | 121 | 133 |
| Earnings before interest and income tax expense | 806 | 1,350 |
| Add: rent expense | 190 | 154 |
| Less: estimated depreciation on capitalized operating leases ¹ | (101) | (83) |
| Net operating profit | 895 | 1,421 |
| Less: estimated income tax expense | (341) | (561) |
| Net operating profit after tax | \$554 | \$860 |
| Average total assets | \$8,332 | \$9,275 |
| Less: average non-interest-bearing current liabilities | (3,062) | (2,892) |
| Less: average deferred property incentives | (549) | (521) |
| Add: average estimated asset base of capitalized operating leases ² | 1,388 | 1,117 |
| Average invested capital | \$6,109 | \$6,979 |

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| | | | | |
|------------------|-----|---|------|---|
| Return on assets | 5.1 | % | 7.9 | % |
| ROIC | 9.1 | % | 12.3 | % |

¹ Capitalized operating leases is our best estimate of the asset base we would record for our leases that are classified as operating if they had met the criteria for a capital lease or we had purchased the property. Asset base is calculated as described in footnote 2 below.

² Based upon the trailing 12-month average of the monthly asset base. The asset base for each month is calculated as the trailing 12 months of rent expense multiplied by eight. The multiple of eight times rent expense is a commonly used method of estimating the asset base we would record for our capitalized operating leases described in footnote 1.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.
(Continued) (Dollar and share amounts in millions except per share and per square foot amounts)

LIQUIDITY AND CAPITAL RESOURCES

We strive to maintain a level of liquidity sufficient to allow us to cover our seasonal cash needs and to maintain appropriate levels of short-term borrowings. We believe that our operating cash flows, available credit facilities and potential future borrowings are sufficient to finance our cash requirements for the next 12 months and beyond.

Over the long term, we manage our cash and capital structure to maximize shareholder return, maintain our financial position, manage refinancing risk and allow flexibility for strategic initiatives. We regularly assess our debt and leverage levels, capital expenditure requirements, debt service payments, dividend payouts, potential share repurchases and other future investments. We believe that as of July 30, 2016, our existing cash and cash equivalents on-hand of \$892, available credit facilities of \$800 and potential future operating cash flows and borrowings will be sufficient to fund these scheduled future payments and potential long-term initiatives.

Operating Activities

Net cash provided by operating activities increased \$436 for the six months ended July 30, 2016, compared with the same period in 2015, primarily due to favorable changes in working capital, which includes our efforts to align inventory levels with sales trends, partially offset by a decrease in earnings.

Investing Activities

Net cash used in investing activities was \$374 for the six months ended July 30, 2016, compared with net cash used of \$581 for the same period in 2015, primarily due to a decrease in capital expenditures related to lower spend on full-line store openings and relocations and our East Coast Fulfillment Center which was completed during the third quarter of 2015.

At the beginning of the second quarter, we completed a review of our five-year capital plan, resulting in approximately \$400, or 10%, of reduced spend primarily related to new stores and remodels over the next few years.

Financing Activities

Net cash used in financing activities was \$180 for the six months ended July 30, 2016, compared with \$238 for the same period in 2015, primarily due to a decrease in share repurchases, partially offset by a decrease in cash book overdrafts.

Free Cash Flow (Non-GAAP financial measure)

Free Cash Flow is one of our key liquidity measures, and when used in conjunction with GAAP measures, provides investors with a meaningful analysis of our ability to generate cash from our business. For the six months ended July 30, 2016, we had Free Cash Flow of \$298 compared with (\$263) for the six months ended August 1, 2015.

Free Cash Flow is not a measure of financial performance under GAAP and should be considered in addition to, and not as a substitute for, operating cash flows or other financial measures prepared in accordance with GAAP. Our method of determining non-GAAP financial measures may differ from other companies' methods and therefore may not be comparable to those used by other companies. The financial measure calculated under GAAP which is most directly comparable to Free Cash Flow is net cash provided by operating activities. The following is a reconciliation of net cash provided by operating activities to Free Cash Flow:

| | Six Months Ended July 30, August 1, 2016 2015 | |
|---|--|----------|
| Net cash provided by operating activities | \$851 | \$415 |
| Less: capital expenditures | (407) | (521) |
| Less: cash dividends paid | (128) | (142) |
| Less: change in credit card receivables originated at third parties | — | (64) |
| (Less) Add: change in cash book overdrafts | (18) | 49 |
| Free Cash Flow | \$298 | (\$263) |
| Net cash used in investing activities | (\$374) | (\$581) |

Net cash used in financing activities (180) (238)

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.
(Continued) (Dollar and share amounts in millions except per share and per square foot amounts)

Credit Capacity and Commitments

As of July 30, 2016, we had total short-term borrowing capacity of \$800 under our senior unsecured revolving credit facility ("revolver") that expires in April 2020, with an option to extend for an additional year. Under the terms of our revolver, we pay a variable rate of interest and a commitment fee based on our debt rating. The revolver is available for working capital, capital expenditures and general corporate purposes. We have the option to increase the revolving commitment by up to \$200, to a total of \$1,000, provided that we obtain written consent from the lenders. From time to time we utilize our commercial paper program to fund working capital needs, which has the effect of reducing our available liquidity under the revolver until repaid.

As of July 30, 2016, we had no issuances outstanding under our commercial paper program and no borrowings outstanding under our revolver.

Impact of Credit Ratings

Under the terms of our revolver, any borrowings we may enter into will accrue interest for Euro-Dollar Rate Loans at a floating base rate tied to LIBOR, for Canadian Dealer Offer Rate Loans at a floating rate tied to CDOR, and for Base Rate Loans at the highest of: (i) the Euro-Dollar rate plus 100 basis points, (ii) the federal funds rate plus 50 basis points and (iii) the prime rate.

The rate depends upon the type of borrowing incurred, plus in each case an applicable margin. This applicable margin varies depending upon the credit ratings assigned to our long-term unsecured debt. At the time of this report, our long-term unsecured debt ratings, outlook and resulting applicable margin were as follows:

| | Credit Ratings | Outlook | Base Interest Rate | Applicable Margin |
|-------------------|-------------------|----------|-----------------------|----------------------|
| Moody's | Baa1 | Stable | LIBOR | 1.02 % |
| Standard & Poor's | BBB+ | Negative | CDOR | 1.02 % |
| | | | various | — |

Should the ratings assigned to our long-term unsecured debt improve, the applicable margin associated with any such borrowings may decrease, resulting in a lower borrowing cost under this facility. Should the ratings assigned to our long-term unsecured debt worsen, the applicable margin associated with our borrowings may increase, resulting in a higher borrowing cost under this facility.

Debt Covenants

The revolver requires that we maintain an adjusted debt to earnings before interest, income taxes, depreciation, amortization and rent ("EBITDAR") leverage ratio of less than four times (see the following additional discussion of Adjusted Debt to EBITDAR). As of July 30, 2016, we were in compliance with this covenant.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.
(Continued) (Dollar and share amounts in millions except per share and per square foot amounts)

Adjusted Debt to EBITDAR (Non-GAAP financial measure)

Adjusted Debt to EBITDAR is one of our key financial metrics, and we believe that our debt levels are best analyzed using this measure. Our goal is to manage debt levels to maintain an investment-grade credit rating and operate with an efficient capital structure. In evaluating our debt levels, this measure provides a reflection of our credit worthiness that could impact our credit rating and borrowing costs. We also have a debt covenant that requires an adjusted debt to EBITDAR leverage ratio of less than four times. As of July 30, 2016, our Adjusted Debt to EBITDAR was 2.6, compared with 2.1 as of August 1, 2015. This increase was primarily driven by reduced earnings.

Adjusted Debt to EBITDAR is not a measure of financial performance under GAAP and should be considered in addition to, and not as a substitute for, debt to net earnings, net earnings, debt or other financial measures prepared in accordance with GAAP. Our method of determining non-GAAP financial measures may differ from other companies' methods and therefore may not be comparable to those used by other companies. The financial measure calculated under GAAP which is most directly comparable to Adjusted Debt to EBITDAR is debt to net earnings. The following is a reconciliation of the components of Adjusted Debt to EBITDAR and debt to net earnings:

| | 2016 ¹ | 2015 ¹ |
|---|-------------------|-------------------|
| Debt | \$2,782 | \$3,141 |
| Add: estimated capitalized operating lease liability ² | 1,518 | 1,231 |
| Less: fair value hedge adjustment included in long-term debt | (18) | (30) |
| Adjusted Debt | \$4,282 | \$4,342 |
| Net earnings | \$424 | \$736 |
| Add: income tax expense | 261 | 481 |
| Add: interest expense, net | 121 | 133 |
| Earnings before interest and income taxes | 806 | 1,350 |
| Add: depreciation and amortization expenses | 617 | 541 |
| Add: rent expense | 190 | 154 |
| Add: non-cash acquisition-related charges | 7 | 16 |
| EBITDAR | \$1,620 | \$2,061 |
| Debt to Net Earnings | 6.6 | 4.3 |
| Adjusted Debt to EBITDAR | 2.6 | 2.1 |

¹ The components of Adjusted Debt are as of July 30, 2016 and August 1, 2015, while the components of EBITDAR are for the 12 months ended July 30, 2016 and August 1, 2015.

² Based upon the estimated lease liability as of the end of the period, calculated as the trailing 12 months of rent expense multiplied by eight. The multiple of eight times rent expense is a commonly used method of estimating the debt we would record for our leases that are classified as operating if they had met the criteria for a capital lease or we had purchased the property.

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Item 3. Quantitative and Qualitative Disclosures About Market Risk.

We discussed our interest rate risk and our foreign currency exchange risk in Part II, “Item 7A. Quantitative and Qualitative Disclosures About Market Risk” in our 2015 Annual Report on Form 10-K filed with the SEC on March 14, 2016. There have been no material changes to these risks since that time.

Item 4. Controls and Procedures.

Disclosure Controls and Procedures

As of the end of the period covered by this Quarterly Report on Form 10-Q, the Company performed an evaluation under the supervision and with the participation of management, including our principal executive officer and principal financial officer, of the design and effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) under the Exchange Act). Based upon that evaluation, our principal executive officer and principal financial officer concluded that, as of the end of the period covered by this Quarterly Report, our disclosure controls and procedures were effective in the timely and accurate recording, processing, summarizing and reporting of material financial and non-financial information within the time periods specified within the SEC’s rules and forms. Our principal executive officer and principal financial officer also concluded that our disclosure controls and procedures were effective 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 principal executive officer and principal financial officer, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) or 15d-15(f) of the Exchange Act) during our most recently completed fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II — OTHER INFORMATION

Item 1. Legal Proceedings.

We are subject from time to time to various claims and lawsuits arising in the ordinary course of business, including lawsuits alleging violations of state and/or federal wage and hour and other employment laws, privacy and other consumer-based claims. Some of these lawsuits include certified classes of litigants, or purport or may be determined to be class or collective actions and seek substantial damages or injunctive relief, or both, and some may remain unresolved for several years. We believe the recorded reserves in our Condensed Consolidated Financial Statements are adequate in light of the probable and estimable liabilities. As of the date of this report, we do not believe any currently identified claim, proceeding or litigation, either alone or in the aggregate, will have a material impact on our results of operations, financial position or cash flows. Since these matters are subject to inherent uncertainties, our view of them may change in the future.

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

(c) Repurchases

(Dollar and share amounts in millions, except per share amounts)

The following is a summary of our second quarter share repurchases:

| | 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 ¹ |
|---|--|---------------------------------------|---|--|
| May 2016 (May 1, 2016 to May 28, 2016) | — | \$— | — | \$761 |
| June 2016 (May 29, 2016 to July 2, 2016) | — | — | — | 761 |
| July 2016 (July 3, 2016 to July 30, 2016) | 0.3 | 39.78 | 0.3 | 751 |
| Total | 0.3 | \$39.78 | 0.3 | |

¹ On October 1, 2015, our Board of Directors authorized a program to repurchase up to \$1,000 of our outstanding common stock through March 1, 2017. The actual number, price, manner and timing of future share repurchases, if any, will be subject to market and economic conditions and applicable SEC rules.

Item 6. Exhibits.

Exhibits are incorporated herein by reference or are filed or furnished with this report as set forth in the Exhibit Index on page 29 hereof.

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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.

NORDSTROM, INC.
(Registrant)

/s/ Michael G. Koppel
Michael G. Koppel
Executive Vice
President and Chief
Financial Officer
(Principal Financial
Officer)

Date: August 30, 2016

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NORDSTROM, INC.

Exhibit Index

| Exhibit | | Method of Filing |
|---------|--|-----------------------------------|
| 10.1 | Nordstrom, Inc. Employee Stock Purchase Plan, amended and restated on June 1, 2016 | Filed herewith electronically |
| 10.2 | Form of 2016 Nonqualified Stock Option Grant Agreement, Supplemental Award | Filed herewith electronically |
| 10.3 | Form of 2016 Restricted Stock Unit Award Agreement, Supplemental Award | Filed herewith electronically |
| 31.1 | Certification of Co-President required by Section 302(a) of the Sarbanes-Oxley Act of 2002 | Filed herewith electronically |
| 31.2 | Certification of Chief Financial Officer required by Section 302(a) of the Sarbanes-Oxley Act of 2002 | Filed herewith electronically |
| 32.1 | Certification of Co-President and Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | Furnished herewith electronically |
| 101.INS | XBRL Instance Document | Filed herewith electronically |
| 101.SCH | XBRL Taxonomy Extension Schema Document | Filed herewith electronically |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document | Filed herewith electronically |
| 101.LAB | XBRL Taxonomy Extension Labels Linkbase Document | Filed herewith electronically |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document | Filed herewith electronically |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document | Filed herewith electronically |