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Bruce Cazenave  Nautilus, Inc. - CEO
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Andrew Burns  D.A. Davidson & Co. - Analyst
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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to Nautilus Q2 FY14 conference call.

(Operator Instructions)

As a reminder, this conference is being recorded, Monday, August 4, 2014. I will now like to turn the conference over to Mr. John Mills. Please go ahead, sir.

John Mills  ICR, Inc. - IR

Thank you. Good afternoon, everyone. Welcome to Nautilus’ second-quarter 2014 conference call. Participants on the call from Nautilus are Bruce Cazenave, Chief Executive Officer; Sid Nayar, Chief Financial Officer; and Bill McMahon, Chief Operating Officer. Our earnings release was issued earlier today and may be downloaded from nautilusinc.com on the Investor Relations page. The earnings release includes a reconciliation of the non-GAAP financial measures mentioned in today’s call to the most directly comparable GAAP measures.

Remarks on today’s conference call may include forward-looking statements within the meanings of the securities laws. These statements, including statements concerning the Company’s current or future financial and operating trends, anticipated new product introductions, available supply of certain products, planned and anticipated results of facility initiatives, and forecasts related to international sales are subject to a number of risks and uncertainties, and actual results may differ materially from those statements.

For more information about these risks, please refer to our quarterly and annual reports filed with the SEC, as well as the Safe Harbor statement in today’s press release. Nautilus undertakes no obligation to publicly update any forward-looking statements to reflect new information, events, or circumstances after they are made, or to reflect the occurrence of unanticipated events unless otherwise indicated. All information and comments regarding our operating results pertain to our continuing operations.

And with that, is my pleasure to turn the call over to Bruce. Go ahead, Bruce.
Bruce Cazenave - Nautilus, Inc. - CEO

Thank you, John. Good afternoon, everyone, and thank you for joining our call today. On today’s call we would like to start by providing a general overview of the second quarter -- I will provide a general overview of the second quarter, and then we’ll turn it over to Sid Nayar to review our financial results in more detail. Bill McMahon will then add some details on each business, as well as updates on product activity. I will then close with some summary remarks before we open up the calls for questions.

During the second quarter, we continued executing on our key areas of focus and are pleased to report solid financial results across all aspects of our business. We achieved top-line growth of 34%, which reflects double-digit growth for both our direct and retail segments. The new Bowflex MAX Trainer product line, which was introduced early in January, performed well in the quarter, and, therefore, we continue to be encouraged about the product line’s long-term potential.

We also improved gross margins in both businesses and, on a consolidated basis, margins increased 320 basis points over the second quarter of last year. Bottom line, it is very gratifying that the business generated positive operating income in our slowest seasonal and, historically, most profit-challenged quarter. As you will hear from Sid, operating income improved by $4.1 million in the second quarter to a positive $2.4 million, compared to a loss of $1.7 million in the second quarter of last year.

As we begin the second half of the year, our team remains focused on the same three key areas that enabled us to deliver substantial improvements in operating performance over the past few years: new product innovation; margin improvement; and generating increased operating leverage as our business grows. At this time, I’d like to turn it over to Sid Nayar, our Chief Financial Officer, who will provide some additional details about the second-quarter financials. Sid?

Sid Nayar - Nautilus, Inc. - CFO

Thank you, Bruce. I would like to review the details of our financial results for the second quarter of 2014. Net sales for the second quarter totaled $48.5 million, an increase of 34% as compared to the same period in the prior year. Year-to-date net sales for 2014 totaled $120.5 million, up 26.2% as compared to net sales of $95.5 million for the same period last year. Second-quarter gross margins increased 490 basis points in the retail segment, and 410 basis points in the direct segment, to 24.4% and 61.7%, respectively, when compared to the same quarter last year.

On an overall basis, total Company gross margins improved to 51%, up 320 basis points versus prior year. For the first half of 2014, total gross margins improved to 52.5%, up 220 basis points as compared to the same prior period. Total operating expenses for the second quarter as a percentage of sales decreased to 46.1% from 46.6% in the same period last year, underscoring ongoing initiatives to leverage operating expenses as our business grows. At this time, I’d like to turn it over to Sid Nayar, our Chief Financial Officer, who will provide some additional details about the second-quarter financials. Sid?

The improvement in operating expenses as a percentage of sales was primarily due to lower media expense in the disproportionately larger growth in the retail business this quarter, as that business carries a much lower variable sales and marketing expense.

Operating expenses for the six months ended June 30, 2014, as a percentage of sales, totaled 43.1% as compared to 45.8% for the same period last year. General and administrative expenses were $5 million, or 10.2% of sales, for the second quarter of 2014, which compares to $4 million, or 11% of sales, in the same period last year. The increased dollar spending in G&A primarily reflects higher spending for fees related to international intellectual property registration and increased legal costs for patent enforcement cases. The improvement in G&A as a percentage of sales highlights favorable operating efficiencies and our ability to leverage the existing platform as the business expands.

General and administrative expenses for the first half of 2014, as a percentage of sales, totaled 8.9% as compared to 9.4% for the same prior period. Research and development costs in the second quarter of 2014 were at $1.8 million, or 3.6% of net sales, compared to $1.3 million, or 3.6% of net sales, in the same period last year. The dollar increase reflects our ongoing commitment to invest in product development and engineering resources required to innovate and broaden our product portfolio through new and refreshed products.
Research and development costs for the first six months of 2014 totaled $3.7 million, or 3% of net sales, as compared to $2.4 million, or 2.5% of net sales, for the same prior period. Operating income for the second quarter of 2014 increased to $2.4 million, as compared to a loss of $1.7 million in the same quarter of last year. The increase reflects higher sales and gross margins in both direct and retail segments, combined with improved operating leverage of sales and marketing and general and administrative expenses.

Operating margin for the second quarter of 2014 improved to 4.9%, compared to a loss of 4.8% for the same period last year. We are pleased to be reporting positive operating income in our seasonally softest quarter of the year. For the first six months of 2014, operating income totaled $11.4 million, or 9.5% of net sales, up 167% compared to the same period last year. Pretax income from continuing operations for the second quarter of 2014 was $2.3 million, or $0.07 per diluted share, compared to a loss of $1.6 million, or $0.05 loss per diluted share, in the same period last year.

Pretax income from continuing operations for the first half of 2014 totaled $11.3 million, or $0.36 per diluted share, compared to $4.3 million, or $0.14 per diluted share, in the comparable period last year. Beginning in the first quarter of 2014, the Company started to report income taxes at a normalized rate following the partial reversal of its valuation allowances in 2013. We believe that pretax income comparisons provide a useful metric to gauge underlying business performance. Given the Company’s US net operating loss carry-forward position, we expect to have minimal cash tax payments in the near term.

Net income from continuing operations for the second quarter of 2014 was $1.5 million, or $0.05 per diluted share. Net income from continuing operations for the second quarter of 2013 was $32.7 million, or $1.04 per diluted share. This includes a $34.3 million, or $1.09 per diluted share, net income tax benefit due to a partial reversal of a valuation allowance recorded against the Company’s deferred tax assets.

Net income from continuing operations for the first half of 2014 totaled $7.2 million, or $0.23 per diluted share. This compares to net income for continued operations of $38.2 million, or $1.22 per diluted share, including the one-time tax benefit I just mentioned, for the first six months of 2013. Total net income, including discontinued operations, for the second quarter of 2014 was $0.6 million, or $0.02 per diluted share. This includes a $0.9 million loss net of taxes, or $0.03 loss per diluted share, from discontinued operations.

This compares to the second quarter last year where we reported total net income, including discontinued operations, of $32.9 million, or $1.05 per diluted share, which included income from discontinued operations of $0.2 million net of taxes, or $0.01 income per diluted share. Total net income for the first half of 2014 was $6 million, or $0.19 per diluted share, compared to $38 million, or $1.21 per diluted share, for the same prior period, which included the one-time income tax benefit previously mentioned.

Turning now to our segment results, net sales in the direct business totaled $32.4 million for the second quarter of 2014, a 27.8% increase over the same quarter last year. Direct segment sales benefited from strong demand for our cardio products, primarily driven by sales of the Bowflex MAX Trainer product line that was launched during Q1 2014. This growth was partially offset by the continued decline of strength products in the direct channel as we continue to see some of these products cascade into the retail business.

Net sales for the first half of 2014 in the direct segment totaled $83.1 million, up 22.3% of the same period last year, driven primarily by the continued strength of the Bowflex TreadClimber category, and the launch of the Bowflex MAX Trainer product. US credit approval rates rose to 38.8% in the second quarter of 2014, up from 33.8% for the same period last year, contributable to several factors, including our media strategy focused on driving quality customer leads and an expanded ladder base.

Gross margin for the direct business improved to 61.7% for the second quarter of 2014, compared to 57.6% in the same quarter of last year. The direct business gross margin benefited from overall overhead operating efficiency in product cost improvements, coupled with favorable product mix. Operating income for the second quarter of 2014 in our direct business was $3.9 million, compared to $0.5 million in the same quarter prior year. Operating income benefited from higher gross margins and improved leverage selling and marketing expenses as a percentage of sales in the second quarter of 2014.

Net sales in our retail segment for the second quarter of 2014 were $15 million, an increase of 47.8% compared to $10.2 million in the second quarter of last year. The improvement reflects strong retailer and consumer acceptance of the Company’s new lineup of cardio products. Additionally,
retail sales in the second quarter of 2013 were muted by retailers deferring purchases awaiting the launch of the Schwinn cardio product introductions that were slated for the third quarter of 2013.

For the first six months of 2014, net sales for the retail segment totaled $35.1 million, an increase of 38.9% over the same period last year. Gross margins for the retail business increased by 490 basis points, to 24.4% in the second quarter 2014, as compared to 19.5% for the prior period, driven by the mix of new products and improved overall overhead operating efficiency. In the second quarter of 2014, operating income for the retail business increased to $1.3 million, as compared to $0.1 million in the same period of last year.

Now turning to the consolidated balance sheet, we continue to improve our financial position. Cash, cash equivalents, and marketable securities increased to $57.3 million as of June 30, 2014, with no debt. This compares to $41 million in cash, cash equivalents, and marketable securities, and no debt, at the end of 2013.

Inventories were $23.2 million as of June 30, 2014, compared to $15.8 million at the end of 2013. The increase in inventory reflected several factors, including pre-buying to allow for the disruption of production related to a planned factory expansion by a supplier and the potential for work stoppages at certain West Coast ports.

Trade payables were $32 million as of June 30, 2014, compared to $37.2 million at the end of 2013. Capital expenditures totaled $0.5 million for the quarter, and we anticipate spending $3.3 million to $3.8 million for the year.

At this time, I would like to turn it over to Bill McMahon, our Chief Operating Officer, who will provide additional insights into our business and key products. Bill?

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Bill McMahon - Nautilus, Inc. - COO

Thank you, Sid. I’d like to provide additional background on our second-quarter results and the overall position of our business. Starting with our direct business, as Sid just outlined, we made good progress in this segment in the second quarter, which is, historically, our softest quarter of the year, and we delivered strong sales in operating income growth.

We continue to see favorable gains in consumer financing approval rates. And these conditions, combined with strong creative performance and a reasonable media cost environment, are allowing us to increase our advertising spend and associated lead generation, which, in turn, is fueling our growth.

In the second quarter, we continue to be very pleased with the performance of the Bowflex MAX Trainer. In the first six months since its launch, we’ve seen strong consumer interest in, and demand for, the product. Importantly, we’ve also received positive feedback from our customers that have purchased the MAX Trainer, along with a growing assortment of favorable reviews.

Earlier this month, we announced that the International Design Awards committee awarded Nautilus a first-place award in the outdoor exercise equipment competition for our MAX Trainer. The annual IDA competition recognizes, honors, and promotes visionaries in product design on a global level.

IDA honorary juries examined over 1,000 entries submitted by architects, and designers of interiors, fashion, products, and graphics, from 52 countries around the world. The IDA award is a great honor and a testament to the efforts of our entire product design team as we continue to focus on creative innovative -- creating innovative fitness solutions to help our customers reach their fitness goals.

Also [ensuring and] encouraging that the MAX Trainer will continue to be an important addition to our product portfolio and a key contributor to our long-term growth, our supply chain capacity has been significantly ramped in response to early sales. We are confident now in our ability to meet demand within our normal shipment windows moving forward. As such, we’ll continue to accelerate our media spend for MAX Trainer advertising, and this will be a significant investment area for us in the back half of 2014.
Our other cardio products, most notably TreadClimber, continue to perform well in Q2. A key element of our MAX Trainer and TreadClimber strategies is to minimize potential cannibalization in media efficiency or sales between the two products. Our results to date, as measured by category sales, media ROI, and responder demographics, would indicate that our creative positioning is effective in achieving our goals.

Meanwhile, as Sid noted, we continue to see a decline in direct strength category sales. While all these declines in actual dollars are becoming a very small percentage of our direct business overall, we still believe there’s an opportunity in this category. Our research indicates that consumer participation rates in strength-related activities remain strong. In response, we have dedicated research and development efforts towards solutions. And, as a result of these efforts, in late 2014, we plan to launch the Bowflex 560 dumbbell with 3DT technology.

This product will be a premium version of our current SelectTech 552 dumbbell and be the first upgrade to this very successful product line in six years. The Bowflex 560 dumbbell will feature a new, innovative design, along with connectivity for repetition and weight-use counting, the ability to download coaching videos with new exercises, and results tracking. The Bowflex 560 dumbbell will launch initially in direct and, later in 2015, in partnership with select retail accounts.

Turning now to our retail business, retail customer response to our new lineup that launched in the fall of 2013 continues to be positive. The success that we had with the Schwinn exercise bikes and elliptical machines gives us confidence that we will have strong products in the pipeline that will perform on the retail floor.

Our retail business has grown an average of 49% over prior year the past four quarters. This success was driven by our innovative line of Schwinn products and the early adoption and selling of those products. It’s important to note now that we are entering into a period of sales comparisons to those previous large gains.

In Q3, 2013, our retail business grew over 70% alone. Thus, our growth challenge in Q3 2014 is more difficult. We remain committed to our long-range growth plans by channel, and it remains our desire to grow each channel year over year, as Bruce has consistently articulated in prior discussions. And there is ample ground for continued growth in retail as our market share, despite our gains in the past year, is still a single-digit percentage. This continued growth will be fueled by product innovation.

In our May earnings call, we outlined several new product launches in the retail channel for the back half of 2014. Our Nautilus line of cardio products and our new selection of treadmills continue to advance forward towards launch this fall. We feel these additional products, combined with the successful model year 2013 Schwinn cardio line as a baseline, provide us with the compelling products necessary to continue to gain market share moving forward.

Based on our current knowledge of major account merchandising and purchasing plans, we feel we will continue to gain share as measured by SKUs, doors, and sales in the second half of 2014 through the growth -- though the growth trajectory will understandably not be at the same pace as seen versus much lower comparisons in the first half 2014.

Finally, in regards to our retail business, our sales internationally defined as sales outside of the US and Canada, continued to increase in the second quarter. We continue to focus on leveraging our globally recognized brands, combined with product that is compliant with international standards, to grow in the international market. Based on current knowledge of accounts and purchasing planning, we anticipate continued strong performance internationally in the second-half 2014.

In the fall of 2013, we conducted a new product showcase event in New York City where we demonstrated the MAX Trainer in model year 2013 Schwinn products. That event generated quite a bit of interest in our products in the social-media and product-review communities. As such, we plan to repeat this event in early October, once again in New York City. We plan to show the Bowflex 560 dumbbell, as well as our new line of treadmills, and the Nautilus model year 2014 products. More information on this event will be forthcoming.

Turning now to inventory. As Sid noted, our inventory position at the end of Q2 2014 was significantly higher than the same period in 2013. Supporting growth in both of our businesses will require an elevated level of inventory moving forward.
However, we caution against using year-over-year comparisons to draw conclusions on future performance. Our current inventory level is intentionally elevated to support several business factors, including the launch of our new, second US distribution center, which will occur in the third quarter, along with some buy ahead of certain key, high-velocity retail products in anticipation of a supplier factory move. We plan to return to a normal, albeit higher than in the past, inventory position later this year, and we continue to closely monitor our purchasing and balance sheet position.

As I previously noted, our second US-based distribution center will go live in the third quarter. This leased facility, located in Columbus, Ohio, will enable us to greatly improve service levels throughout the United States. Our normal shipping time to a customer will move from 10 days to less than 5 days. We will incur some initial greater ongoing expense for this facility but, over time, we expect operational efficiencies and improved customer-service levels to offset cost.

Lastly, in regards to commercial brand licensing, our previous commercial licensing partner for the Nautilus brand, Med-Fit Systems, has been sold to Core Health and Fitness, makers of the Star Trac and StairMaster products. We have entered into a new licensing agreement for commercial strength products branded under the Nautilus name with Core. We are pleased with this change since we feel Core is better equipped in terms of size, capital, and global presence to drive growth for the Nautilus brand in the commercial space while providing elevated service levels to long-time accounts. We have a long history of successful partnership with Core, and we are optimistic that the Nautilus brand will be well represented in the commercial club market under this new agreement.

In summary, we have great momentum across all aspects of our business as we begin the back half of 2014. Our foundation has improved tremendously over the past few years, with our expanded product portfolio, improved product margins, and enhanced operating platform. We remain focused on continued innovation, and we’re excited about what we have in the pipeline.

And now I’d like to turn the call back over to Bruce for his final comments. Bruce?

Bruce Cazenave - Nautilus, Inc. - CEO

Thank you, Bill. Before opening up the call for questions, I would like to make a few final summary comments. We are pleased with where we are as a company, in terms of traction on key initiatives and with the trajectory of improved profitability over the last few years. Our ability to consistently deliver growth well above the industry average, along with improved financial results, reflects our team’s focus and ability to execute well. As mentioned previously, we understand and constantly remind ourselves that, despite the significant progress over the last few years, we are not yet where we want to be -- and should be -- in terms of profitability, consumer access, and presence in the global market.

Importantly, we continue to identify and pursue additional strategic growth drivers, including consumer insight-driven, new product innovation; capitalizing on international growth opportunities; and layering in other new market approaches. Also -- and I can’t emphasize it enough -- that we are and will continue to make the necessary investments in our infrastructure to support the goal of profitably expanding our business and positioning Nautilus for further long-term growth.

I’m extremely proud of our team and for all the accomplishments to date. And, thanks to their efforts, we are well positioned for the upcoming peak fitness season. That concludes our prepared remarks. Now, I’d like to open up the call for questions. Operator?

QUESTIONS AND ANSWERS

Operator

Thank you.

(Operator Instructions)

Our first question comes from Reed Anderson with Northland Securities.
Reed Anderson - Northland Securities, Inc. - Analyst
Good afternoon. Thanks for taking the questions, and congratulations on a terrific quarter.

Bruce Cazenave - Nautilus, Inc. - CEO
Thank you, Reed; good afternoon.

Reed Anderson - Northland Securities, Inc. - Analyst
I think you have to go back almost 10 years to a time when you actually made that kind of money in the second quarter, so that's great. A couple questions: I'm not sure who wants to take it, but obviously, from a MAX standpoint, we're caught up now in terms of fulfilling demand, et cetera. I'm just curious: At what point did you get there? Was it towards the end of the second quarter, or was it more July when you got to where you were able to meet orders on the normal time frame?

Bill McMahon - Nautilus, Inc. - COO
It was in the back third of the quarter, Reed. This is Bill. And we were caught up before the end of the quarter.

Reed Anderson - Northland Securities, Inc. - Analyst
Super. And then, in terms of the retail side -- obviously, terrific, or better than I had been thinking. You do have the real tough comparison though. But I'm just curious: If you think about the retail on a half basis, do you think that retail in the second half -- so the six-month, second half -- do you think that will grow over last year? Or do you think it's going to be tough because of the comparison?

Bruce Cazenave - Nautilus, Inc. - CEO
Reed, this is Bruce. It will be tough, and certainly a lot tougher than the lower comps we had in the first half of the year. But our expectations are, because of the traction -- continued traction -- on the product that we introduced last fall, plus the new things that Bill's described we're layering on top of that, that we should be able to continue to generate growth in the back half. Although I have to qualify and say that it's going to be at a more modest level than the significant increases we posted in the first half.

Reed Anderson - Northland Securities, Inc. - Analyst
That makes a lot of sense. And then, a couple more: On the licensing side -- that ticked up a little better than I was thinking. There's some planning nuances once in a while there, so I'm just curious: Has anything changed there, because I think, more or less, we were thinking it was going to be flattish this year. So, I'm wondering if you've had any new license arrangements or if that reflects some different pricing or something -- just curious what might be going on there?

Sid Nayar - Nautilus, Inc. - CFO
Reed, this is Sid. In the second quarter, we saw some strong sales from some of our royalty licensees, which were partially offset by the transition to our new commercial fitness brand. We sort of have limited visibility into whether that royalty stream will be as strong the second half of the year, although we do know that the Nautilus Marshall transition will pose a drag on second-half comps.
Reed Anderson - Northland Securities, Inc. - Analyst
Okay. Got it. That makes a lot of sense. Good. All right. I'll let somebody else jump in, and I'll come back in a little bit. Best of luck. Thanks, guys.

Bruce Cazenave - Nautilus, Inc. - CEO
Thank you, Reed.

Operator
The next question comes from Lee Giordano with CRT Capital.

Lee Giordano - CRT Capital - Analyst
Thank you. Good afternoon, everybody.

Bruce Cazenave - Nautilus, Inc. - CEO
Hi, Lee.

Lee Giordano - CRT Capital - Analyst
Hi. So, on the gross margins -- very impressive gains here in the quarter. I was just wondering if you could talk a little more about what drove that -- maybe quantify how much of that was mix? And then, how should we think about gross margin going forward in the back half of the year? Thanks.

Sid Nayar - Nautilus, Inc. - CFO
Lee, this is Sid. And I'll split it into the gross margins by channel. In the direct, I think we've indicated previously that we continue to believe that gross margins for the direct segment are optimal in the low-60%s. Several factors, including the mix of product and mix within product, will influence that number from quarter to quarter, but we still remain comfortable within that range for the direct channel.

In the retail channel, again, margins are fairly greatly influenced by domestic versus international channel sales, and the product and customer mix. And we are continuing to strive to introduce products that are accretive from a margin perspective. In that channel, the prior margins were negatively impacted by some promotional activity, and I think we are focused on achieving margins in the mid-20% range or better in the retail channel as well.

Lee Giordano - CRT Capital - Analyst
Great. Thank you.

Operator
(Operator Instructions)
Our next question comes from Andrew Burns with D.A. Davidson.

Andrew Burns - D.A. Davidson & Co. - Analyst

Thanks, and congratulations on year-to-date performance. I had just a point of clarification here on some comments around operating expenses. There was a comment of accelerating marketing expenses, and also some heightened distribution expenses tied to the new facility there. Could you speak to the magnitude of those changes, and is it significant enough to be disruptive to the margins we’ve been seeing as of late? Thanks.

Bill McMahon - Nautilus, Inc. - COO

Hey, Andrew. This is Bill. We do not expect these investments to be disruptive to our margin path that we’re aiming for. I can tell you on the new distribution center, some initial cost is primarily capital expense, and it’s in the high six figures.

And on the media investment, even though we will be ramping up spending against MAX, we still manage that spend as we do against all new products against reasonable return-on-investment targets that we’ve set. So, while we will be increasing spending, I wouldn’t anticipate a fundamental change in direction in our margin structure.

Andrew Burns - D.A. Davidson & Co. - Analyst

Thanks. And then, just at a high level, I was hoping you could speak to your product pipeline. And we’ve seen connectivity being a growing theme here, and it was highlighted on the 560 dumbbell and certainly incorporated in the Max Trainer -- just your long-term view of how important that is to differentiate your product and lead the market? Thanks.

Bill McMahon - Nautilus, Inc. - COO

Well, Andrew -- Bill again. We believe that a digital strategy is absolutely critical to our direction moving forward. We know, based on our research and just, frankly, general trends in the market, that consumers are wanting to not just have a console that tells them how many miles they went. They want to know what were the results of that effort, and how does that compare to how I did last week, last month, last year. If you provide them with those solutions, then they’re more satisfied with the product and more likely to use it.

So, we feel like this has to become a fundamental part of our Business going forward. And most products we launch will have some element of digital in them, whether it’s an app or actual integration in the product that elevates our game from where it was in the previous line of products. So, our pipeline is -- we just finished our strategic planning where we look at our product pipeline out over three years, and we still have a full pipeline of ideas that we’re excited to be working on right now.

Andrew Burns - D.A. Davidson & Co. - Analyst

Okay. Thanks. And good luck.

Bruce Cazenave - Nautilus, Inc. - CEO

Thank you, Andrew.

Operator

(Operator Instructions)
Our next question comes from Ian Corydon with B. Riley & Co.

Ian Corydon - B. Riley & Company - Analyst

Thank you. Understanding you’re up against tough retail comparisons in the back half, it seems like if you take the direct performance in the first half and extrapolate that same performance through in the back half, your overall operating margin for FY14 would reach -- looks like comfortably into the double digits. Does that line of reasoning make sense?

Bruce Cazenave - Nautilus, Inc. - CEO

Ian, hi. You know we don’t give guidance, either for the quarter or for the year. I would say that, similar to what we were describing for retail, in terms of the comps that we face, we also have some tough comps coming up on the direct side as well. So, it’s always difficult at this time of the year to kind of project out, with so much of the volume being done in the -- particularly in the fourth quarter -- in the late fourth quarter. So, I would say that we’re on a good trajectory in both businesses, but, again, to extrapolate the kind of growth that we’ve posted, either in direct and retail for the first half, would be a real stretch, if you extended that linearly to the back half.

Ian Corydon - B. Riley & Company - Analyst

Okay.

Bruce Cazenave - Nautilus, Inc. - CEO

We still plan to grow both businesses in the back half.

Ian Corydon - B. Riley & Company - Analyst

What are the tough comps in direct in the back half?

Bruce Cazenave - Nautilus, Inc. - CEO

Well, particularly the fourth quarter, if you look at the fourth quarter -- I can’t -- I don’t have at my fingertips what it was over the prior year, but the revenue growth in the fourth quarter I think was significant.

Ian Corydon - B. Riley & Company - Analyst

Okay. Thank you.
Reed Anderson - Northland Securities, Inc. - Analyst

Hi. Bill, in your prepared remarks, you made a comment -- I wrote down you said reasonable media environment or something like that. So, I'm just curious: Is that what you were expecting, or are you benefiting a little more than you thought? Just want a little more color on what you meant by that.

Bill McMahon - Nautilus, Inc. - COO

As you know, Reed, we buy in the scatter market, and so we're highly dependent on what happens to the larger players in the media world. And right now, conditions -- I wouldn't say they're favorable. I'd say they're about what we expected, but we're not really encountering headwinds in media buying either. So, there's no significant events going on like, say, an Olympics or elections that -- or at least national elections that sometimes get in the way of our buying pattern.

Reed Anderson - Northland Securities, Inc. - Analyst

That makes sense. And the other follow-up I had was: On the DC that's going to open here in 3Q, are you going to fulfill both your businesses out of that, or just one or the other? It wasn't clear exactly.

Bill McMahon - Nautilus, Inc. - COO

No, we will divide -- we will maintain our Portland distribution center as well, for generally west coast. We've done some outbound shipping assessments with our partners, and we feel we have an optimal map for fulfillment.

Reed Anderson - Northland Securities, Inc. - Analyst

Okay. That's great. Okay. That's a lot, guys.

Bruce Cazenave - Nautilus, Inc. - CEO

Thank you, Reed.

Operator

There are no further questions over the phone lines at this time. I'll turn the call back over to you.

Bruce Cazenave - Nautilus, Inc. - CEO

Great. Thank you. Thanks again, everyone, for your participation and interest in our call today. As Bill mentioned, we are planning another new product showcase in New York in early October for our media partners, and our investor community will be invited to part of that event as well. We hope to see you there, and either way, we look forward to speaking with you on our next, third-quarter 2014 conference call, which will be scheduled in the November time frame. Have a great rest of the day. Thank you, all. Bye-bye.

Operator

Ladies and gentlemen, that does conclude the conference call for today. We thank you for your participation, and ask that you please disconnect your line.