BEST BUY CO INC

FORM 10-Q/A
(Amended Quarterly Report)

Filed 03/20/00 for the Period Ending 07/28/99

Address	7601 PENN AVE SOUTH RICHFIELD, MN 55423
Telephone	6122911000
CIK	0000764478
Symbol	BBY
SIC Code	5731 - Radio, Television, and Consumer Electronics Stores
Industry	Retail (Technology)
Sector	Services
Fiscal Year	02/03

BEST BUY CO INC

FORM 10-Q/A
(Amended Quarterly Report)

Filed 3/20/2000 For Period Ending 7/28/1999

Address	7601 PENN AVE SOUTH
	RICHFIELD, Minnesota 55423
Telephone	612-291-1000
CIK	0000764478
Industry	Retail (Technology)
Sector	Services
Fiscal Year	03/01

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q/A
(Amendment Number 1)

(Mark One)

/x/	QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED AUGUST 28, 1999

OR

/ /	TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM TO

Commission File Number: 1-9595

BEST BUY CO., INC.
(Exact name of registrant as specified in its charter)

Minnesota (State or other jurisdiction of incorporation or organization)	41-0907483 (I.R.S. Employer Identification No.)
7075 Flying Cloud Drive Eden Prairie, Minnesota (Address of principal executive offices)	55344 (Zip Code)

(612) 947-2000
(Registrant's telephone number, including area code)

N/A
(Former name, former address and former fiscal year, if changed since last report)

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 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 /x/ No / /**

At August 28, 1999, there were 205,270,000 shares of common stock, $.10 par value, outstanding.

The Registrant's financial statements as of August 28, 1999, February 27, 1999 and August 29, 1998, and for the three and six-month periods ended August 28, 1999 and August 29, 1998 have been restated and are included herein. Items 1, 2 and 6 of the Registrant's Quarterly Report on Form 10-Q are hereby amended in their entirety as follows:

PART 1. FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

BEST BUY CO., INC.

CONSOLIDATED BALANCE SHEETS

ASSETS

($ in 000)

	August 28, 1999 (Unaudited)	February 27, 1999	August 29, 1998 (Unaudited)
CURRENT ASSETS			
Cash and cash equivalents	$ 473,444	$ 785,777	$ 491,632
Receivables	178,492	132,401	140,714
Recoverable costs from developed properties	89,699	73,956	48,045
Merchandise inventories	1,287,646	1,046,366	1,167,966
Other current assets	35,135	33,327	29,537
Total current assets	2,064,416	2,071,827	1,877,894
PROPERTY AND EQUIPMENT			
Land and buildings	48,309	23,158	21,212
Leasehold improvements	187,887	174,495	162,680
Furniture, fixtures and equipment	610,831	505,232	395,360
Property under capital leases	29,079	29,079	29,079
	876,106	731,964	608,331
Less accumulated depreciation and amortization	353,286	308,324	280,137
Net property and equipment	522,820	423,640	328,194
OTHER ASSETS	40,947	36,156	20,581
TOTAL ASSETS	$ 2,628,183	$ 2,531,623	$ 2,226,669

See notes to consolidated financial statements.

BEST BUY CO., INC.

CONSOLIDATED BALANCE SHEETS (continued)

LIABILITIES AND SHAREHOLDERS' EQUITY

($ in 000)

	August 28,		August 29,

	1999 (Unaudited)	February 27, 1999	1998 (Unaudited)
CURRENT LIABILITIES			
Accounts payable	$ 1,058,921	$ 1,011,746	$ 860,116
Accrued compensation and related expenses	68,097	86,667	48,403
Accrued liabilities	261,095	281,215	209,295
Current portion of long-term debt	10,130	30,088	182,078
Total current liabilities	1,398,243	1,409,716	1,299,892
LONG-TERM LIABILITIES	69,743	57,453	54,038
LONG-TERM DEBT	25,690	30,509	35,295
SHAREHOLDERS' EQUITY			
Preferred stock, $1.00 par value:			
Authorized—400,000 shares;			
Issued and outstanding—none	—	—	—
Common stock, $.10 par value:			
Authorized—400,000,000 shares;			
Issued and outstanding 205,270,000, 203,621,000 and 201,540,000 shares, respectively	20,527	10,181	10,077
Additional paid-in capital	527,717	542,377	508,329
Retained earnings	586,263	481,387	319,038
Total shareholders' equity	1,134,507	1,033,945	837,444
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 2,628,183	$ 2,531,623	$ 2,226,669

See notes to consolidated financial statements.

BEST BUY CO., INC.

CONSOLIDATED STATEMENTS OF EARNINGS

($ in 000, except per share amounts)

(Unaudited)

	Three Months Ended		Six Months Ended	
	August 28, 1999	August 29, 1998	August 28, 1999	August 29, 1998
Revenues	$ 2,686,640	$ 2,177,766	$ 5,072,071	$ 4,116,149
Cost of goods sold	2,156,120	1,771,775	4,079,549	3,361,220
Gross profit	530,520	405,991	992,522	754,929
Selling, general and administrative expenses	440,914	337,554	831,215	663,708
Operating income	89,606	68,437	161,307	91,221
Net interest income (expense)	4,276	(1,010)	8,689	(3,505)
Earnings before income tax expense	93,882	67,427	169,996	87,716
Income tax expense	35,815	25,972	65,120	33,784
Net earnings	$ 58,067	$ 41,455	$ 104,876	$ 53,932
Basic earnings per share	$ .28	$ .21	$ .51	$ .27
Diluted earnings per share	$ .27	$ .20	$ .49	$ .26
Basic weighted average common shares outstanding (000's)	205,038	201,029	204,536	196,273

Diluted weighted average common shares outstanding (000's)	213,907	209,852	213,593	208,972

See notes to consolidated financial statements.

BEST BUY CO., INC.

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

FOR THE SIX MONTHS ENDED AUGUST 28, 1999

($ in 000)

(Unaudited)

	Common stock	Additional paid-in capital	Retained earnings
Balance, February 27, 1999	$ 10,181	$ 542,377	$ 481,387
Stock options exercised	333	27,235	—
Tax benefit from stock options exercised	—	65,658	—
Two-for-one stock split	10,190	(10,190)	—
Repurchase of common stock	(177)	(97,363)	—
Net earnings, six months ended August 28, 1999	—	—	104,876
Balance, August 28, 1999	$ 20,527	$ 527,717	$ 586,263

See notes to consolidated financial statements.

BEST BUY CO., INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

($ in 000)

(Unaudited)

	Six Months Ended	
	August 28, 1999	August 29, 1998
OPERATING ACTIVITIES		
Net earnings	$ 104,876	$ 53,932
Depreciation, amortization and other non-cash charges	46,110	36,322
	150,986	90,254
Changes in operating assets and liabilities:		
Receivables	(46,091)	(45,012)
Merchandise inventories	(241,280)	(107,178)
Other assets	(2,263)	7,698
Accounts payable	47,175	97,464
Other liabilities	38,741	1,294

Total cash (used in) provided by operating activities	(52,732)	44,520
INVESTING ACTIVITIES		
Additions to property and equipment	(144,733)	(31,124)
Increase in recoverable costs from developed properties	(15,743)	(39,830)
Increase in other assets	(3,933)	(3,531)
Total cash used in investing activities	(164,409)	(74,485)
FINANCING ACTIVITIES		
Repurchase of common stock	(97,540)	—
Common stock issued	27,125	10,090
Long-term debt payments	(24,777)	(8,620)
Total cash (used in) provided by financing activities	(95,192)	1,470
DECREASE IN CASH AND CASH EQUIVALENTS	(312,333)	(28,495)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	785,777	520,127
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 473,444	$ 491,632

Amounts in this statement are presented on a cash basis and therefore may differ from those shown in other sections of this quarterly report.

Supplemental cash flow information:		
Cash paid during the period for:		
Interest	$ 3,132	$ 12,247
Income taxes	$ 47,064	$ 33,952

See notes to consolidated financial statements.

BEST BUY CO., INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation:

The consolidated balance sheets as of August 28, 1999, and August 29, 1998, the related consolidated statements of earnings for the three and six months then ended, consolidated cash flows for the six months then ended and the consolidated statement of changes in shareholders' equity for the six months ended August 28, 1999, are unaudited; in the opinion of management, all adjustments necessary for a fair presentation of such financial statements have been included and were normal and recurring in nature. The Company's business is seasonal in nature and interim results are not necessarily indicative of results for a full year. These interim financial statements and the related notes should be read in conjunction with the financial statements and notes included in the Company's Annual Report to Shareholders for the fiscal year ended February 27, 1999, and incorporated by reference into the Company's Annual Report on Form 10-K. Certain prior year amounts have been reclassified to conform to current year presentation.

2. Change in Accounting Policy—Performance Service Plans:

The Company sells Performance Service Plans (PSPs) on behalf of an unrelated third party. In December 1999, the staff of the Securities and Exchange Commission (SEC Staff) announced its position with respect to the accounting for revenues from extended service contracts, such as PSPs. The SEC Staff indicated that in those states where a retailer is deemed to be the obligor, net revenues from the sales of service contracts should be recognized over the life of the underlying contract rather than at the time of the sale. The designation of a retailer as the obligor varies depending in large part on applicable state regulations. The Company had, until the third quarter of fiscal 2000, recognized the net commission revenue from the sale of all insured PSPs at the time of sale. The Company began selling insured PSPs in the fourth quarter of fiscal 1996.

Effective as of the beginning of the third quarter of fiscal 2000, the Company has changed its accounting policy with respect to the recognition of revenues from the sale of obligor service contracts. Pursuant to the Company's new policy, the Company recognizes net commission revenues ratably over the terms of the obligor service contracts sold, generally two to five years. The Company has and will continue to recognize net commission revenues for the sale of non-obligor service contracts at the time of sale. The Company has given retroactive effect to this new accounting policy by restating its previously published financial statements beginning with fiscal 1996.

The impact of the restatement on affected financial information in the consolidated statements of operations for the three-month and six-month periods ended August 28, 1999 and August 29, 1998, is as follows (in thousands, except per share amounts):

	Three Months Ended			
	As Previously Reported August 28, 1999 (Unaudited)	As Restated August 28, 1999 (Unaudited)	As Previously Reported August 29, 1998 (Unaudited)	As Restated August 29, 1998 (Unaudited)
Revenues	$ 2,688,183	$ 2,686,640	$ 2,182,124	$ 2,177,766
Cost of goods sold	2,156,120	2,156,120	1,771,775	1,771,775
Gross profit	532,063	530,520	410,349	405,991
Selling, general and administrative expenses	440,914	440,914	337,554	337,554
Operating income	91,149	89,606	72,795	68,437
Income tax expense	36,404	35,815	27,650	25,972
Net earnings	59,021	58,067	44,135	41,455
Basic earnings per share	0.29	0.28	0.22	0.21
Diluted earnings per share	0.28	0.27	0.21	0.20

	Six Months Ended			
	As Previously Reported August 28, 1999 (Unaudited)	As Restated August 28, 1999 (Unaudited)	As Previously Reported August 29, 1998 (Unaudited)	As Restated August 29, 1998 (Unaudited)
Revenues	$ 5,074,371	$ 5,072,071	$ 4,125,788	$ 4,116,149
Cost of goods sold	4,079,549	4,079,549	3,361,220	3,361,220
Gross profit	994,822	992,522	764,568	754,929
Selling, general and administrative expenses	831,215	831,215	663,708	663,708
Operating income	163,607	161,307	100,860	91,221
Income tax expense	66,000	65,120	37,495	33,784
Net earnings	106,296	104,876	59,860	53,932
Basic earnings per share	0.52	0.51	0.30	0.27
Diluted earnings per share	0.50	0.49	0.29	0.26

In addition, the restatement also resulted in changes to the consolidated balance sheets as of August 28, 1999, February 27, 1999 and August 29, 1998 and certain classifications within the statements of cash flows for the six-month periods ended August 28, 1999 and August 29, 1998. As of August 28, 1999, the restatement resulted in a net reduction in retained earnings of approximately $32 million representing the deferral of revenues net of the applicable income tax effect. The revenue deferred under the new policy will be recognized in future years over the lives of the related contracts.

3. Income Taxes:

Income taxes are provided on an interim basis based upon management's estimate of the annual effective tax rate. Management's revised estimate of the annual effective tax rate of 38.3% for fiscal 2000

reflects higher levels of tax exempt interest income. This revised annual estimate resulted in an effective rate of 38.1% for the second quarter.

4. Earnings Per Share:

The following table presents a reconciliation of the numerators and denominators of basic and diluted earnings per common share:

	Three Months Ended		Six Months Ended	
	August 28, 1999	August 29, 1998	August 28, 1999	August 29, 1998
Numerator (000's):				
Net earnings	$ 58,067	$ 41,455	$ 104,876	$ 53,932
Interest on preferred securities, net of tax	—	—	—	771
Net earnings assuming dilution	$ 58,067	$ 41,455	$ 104,876	$ 54,703
Denominator (000's):				
Weighted average common shares Outstanding	205,038	201,029	204,536	196,273
Effect of dilutive securities:				
Employee stock options	8,869	8,823	9,057	8,508
Preferred securities	—	—	—	4,191
Weighted average common shares outstanding assuming dilution	213,907	209,852	213,593	208,972
Basic earnings per share	$ .28	$ .21	$ .51	$ .27
Diluted earnings per share	$ .27	$ .20	$ .49	$ .26

In March 1999, the Company effected a two-for-one stock split in the form of a stock dividend. All common share and per share information reflects the stock split.

5. Credit Facility:

In August 1999, the Company entered into an unsecured $100 million revolving credit facility, replacing the $220 million facility that was scheduled to mature in June 2000. The Company was able to reduce the size of the facility due to improved operating performance and better inventory management. In addition, the new facility makes certain financial covenants less restrictive thereby providing the Company with additional flexibility. The current facility is scheduled to mature in August 2002.

6. Share Repurchase Programs:

In October 1998, the Company's Board of Directors approved the purchase of up to $100 million of the Company's common stock from time to time through open market purchases over the following twelve months. As of August 28, 1999, this repurchase program was completed with a total of 1.8 million shares purchased.

In September 1999, the Company's Board of Directors approved the purchase of up to $200 million of the Company's common stock from time to time through open market purchases. This repurchase program has no stated expiration date.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Results Of Operations

Net earnings for the second quarter of fiscal 2000 were a record $58.1 million, or $.27 per share on a diluted basis, compared to net earnings of $41.5 million, or $.20 per share, for the comparable period last year. For the first six months of the current fiscal year net earnings were a record $104.9 million, or $.49 per share on a diluted basis, compared to $53.9 million, or $.26 per share, for the same period last year. Continued strength in consumer spending and market share gains combined with continued improvement in gross profit margins were the principal factors generating the record results. Pre-opening expenses incurred in connection with the opening of 19 new stores during the quarter reduced net earnings for the second quarter of the current year by approximately $8 million, or $.04 per diluted share. No new stores were opened in the second quarter of fiscal 1999.

Results of operations reflect a change in accounting and restatement of previously reported amounts where necessary to reflect recent Securities and Exchange Commission Staff guidance on accounting for certain extended service contracts, as more fully described in Note 2 to the accompanying financial statements. The Company refers to these contracts as Performance Service Plans (PSPs). Previously reported earnings for the second quarter of fiscal 2000 were $.28 per share before being reduced by $1.0 million, or $.01 per share, to reflect the change. Previously reported earnings for the first six months of fiscal 2000 were $.50 per share before being reduced by $1.4 million, or $.01 per share, to reflect the change. The reduction to retained earnings, as a result of the change, through August 28, 1999, totaled approximately $32 million.

Revenues in the second quarter increased 23% to $2.687 billion compared to $2.178 billion in the second quarter last year. Revenues in the first six months increased 23% to $5.072 billion compared to $4.116 billion last year. Comparable store sales increases of 11.1% for the second quarter and 12.2% year-to-date and a net increase of 43 new stores in the past twelve months drove the revenue increases. The Company's multi-year program to offer a more customer focused product assortment, improve in-stock levels and increase advertising effectiveness, coupled with successful retail execution, has allowed the Company to capitalize on the continued strength in the overall retail sector and generate comparable store sales increases in excess of 10% for seven consecutive quarters. Sales of digital technology products such as Digital Versatile Disc (DVD), Digital Broadcast Satellite (DBS), digital cameras and camcorders, as well as strong sales of personal computers and music and movies, fueled the comparable store sales gains. All major product categories generated comparable store sales increases as the Company continued to gain market share.

As of August 28, 1999, the Company operated 332 stores compared to 289 stores one year ago. In the second quarter, the Company opened 19 new stores, including five new stores in the San Francisco market and the first three of the Company's new small market stores designed to serve markets with populations less than 200,000. The Company also expanded four stores and relocated three stores to larger facilities. The new stores and store expansions were Concept IV stores which feature improved merchandising, signage and customer service and are expected to better address customers' needs as the industry continues to progress into new digital products. The Company plans to open 23 new stores in the third quarter including entry into the new markets of San Diego, California; Jacksonville and Tallahassee, Florida; Richmond and Norfolk, Virginia; Rochester and Albany, New York; and Providence, Rhode Island. In addition, the Company announced plans to open 55 to 60 new stores in fiscal 2001, including entry into the New York metropolitan market with approximately twelve stores.

The Company is investing in building the systems infrastructure, vendor relationships and content base to support its developing e-commerce business, BestBuy.com. The Company is in the process of

recruiting several new executives to fill critical leadership roles in developing its online presence. The Company anticipates introducing expanded product offerings on its website in early calendar 2000. Internet operations are not expected to contribute materially to the Company's total revenues in the current fiscal year.

Retail store sales mix by major product category for the three-month and six-month periods was as follows:

	Three Months Ended		Six Months Ended	
	August 28, 1999	August 29, 1998	August 28, 1999	August 29, 1998
Home Office	36%	36%	36%	36%
Consumer Electronics				
Audio	10	11	10	11
Video	16	15	16	15
Entertainment Software	17	18	18	19
Appliances	11	11	10	10
Other	10	9	10	9
Total	100%	100%	100%	100%

In the home office category, the launch of an Internet Service Provider (ISP) subsidy offer on personal computers in the second quarter represented a significant change in the retailing of personal computers. The ISP subsidy offer quickly became common practice among retailers. The offer provides customers with an instant rebate on the purchase of a personal computer when the customer signs an extended contract to subscribe to Internet service provided by the ISP. This rebate to the customer is funded by the ISP which also bears the risk of collection of the monthly subscriber fees paid by the customer to the ISP. The Company believes it has had a distinct advantage by being able to provide the rebate to the customer at the time of the sale as opposed to utilizing a mail-in rebate used by most other retailers. This program has been successful in driving significant increases in unit volumes of personal computers, particularly the lower price point, entry-level models. The higher volumes have been sufficient to offset the decline in average selling price of computers sold by the Company and resulted in a double-digit comparable store sales increase in the home office category. The increased unit volumes also resulted in higher sales of accessories and performance service plans (PSPs) that accompany the sale of personal computer hardware.

Sales of digital technology products such as DVD, digital camcorders and DBS, as well as strong sales of analog products such as televisions and home theater systems, drove second quarter and year-to-date sales increases in the consumer electronics category. The Company remains the industry leader in DVD hardware sales market share and continues to effectively capitalize on the consumer demand for digital products.

Sales of entertainment software, which includes music and movies, computer software and video games, increased moderately in the second quarter. Sales of compact discs and DVD movies were particularly strong despite a lack of significant new releases. DVD movies outsold VHS movies for the first time in the second quarter due to consumers' rapid acceptance of the DVD format. The Company leads the industry in DVD software sales market share and, by year-end, expects to offer over 2,000 DVD movie titles aided by the expected release of Disney classic cartoon titles beginning in October. Strong sales of music and movies were offset by softer sales of computer software and video games due to declining average selling prices, a lack of new software titles and the anticipated transition to advanced technology game systems in the third quarter.

Management expects that comparable store sales increases could moderate in the future as comparisons become more difficult. Additionally, the Company's revenues are dependent upon adequate quantities of products from the Company's suppliers. While management does not currently expect product

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shortages, events such as natural disasters, component part availability, or supply issues resulting from year 2000 systems issues could impact the availability of product from the Company's suppliers and impact revenues.

Gross profit margin in the second quarter improved to 19.7% compared to 18.6% in the second quarter of fiscal 1999, over a full 1% of sales improvement. Gross profit margin in the six-month period improved 1.3% of sales to 19.6% compared to 18.3% in the same period last year. These improvements reflect the continuing benefit from the Company's initiatives to generate more profitable product assortments, improve inventory management and enhance advertising effectiveness. Increased sales of higher margin PSPs and accessories favorably impacted margins in the quarter and year-to-date periods. Sales of PSPs accounted for 4.2% of total sales for both the second quarter and six-month period of the current year compared to 3.9% and 3.8% for the quarter and six-month period of the prior year, respectively. The Company's ongoing efforts to reduce inventory shrink also contributed to the margin improvements. Management expects gross profit margins will continue to exceed prior year levels in the second half of this year. However, an expected seasonal change will result in a lower gross profit margin in the second half of the year as compared to the first half. This change is due, in part, to a seasonal product sales mix shift, which typically includes more personal computers and fewer appliances and mobile electronics. In addition, promotional activity typically increases during the holiday season and during store grand opening events. The percentage of higher margin PSP sales in the mix declines during the holiday season, also impacting gross profit margins in the second half of the year.

Selling, general and administrative (SG&A) expenses increased to 16.4% of sales in the quarter compared to 15.5% in the second quarter last year. Year-to-date, SG&A expenses increased to 16.4% of sales in the current year compared to 16.1% for the same period last year. These increases were largely due to hiring and training costs associated with the opening of 19 new stores during the quarter, as well as significant grand opening advertising costs associated with the entry into the San Francisco market. The pre-opening costs of approximately $450,000 per store plus the grand opening advertising expenses increased second quarter SG&A expenses by approximately $13 million, or 0.5% of sales, compared to the same period last year. Of the 19 new stores opened in the current year's second quarter, ten were opened in the last month of the quarter. As a result, the benefits of the pre-opening costs incurred in opening those stores will not be fully realized until the second half of the year. The remainder of the increase in SG&A spending was due principally to expenses incurred to support the Company's increased expansion plans, as well as investments in personnel and strategic initiatives expected to produce longer-term benefits. These costs include training and development of retail store management, developing the Company's e-commerce business and enhancing systems that support retail and service operations. Excluding the impact of the new store opening costs, SG&A expenses as a percentage of gross margin declined to 81% in the second quarter as compared to 83% in the second quarter last year, and operating margin improved to 3.8% compared to 3.1% in the same quarter one year ago. This leverage is consistent with management's intent to fund expansion and business improvement initiatives through increased gross profit margins. Management currently expects that SG&A spending will continue to increase on a year-over-year basis. Higher sales volumes in the second half of the year, combined with higher year-over-year gross margin rates, are expected to result in improved operating income margins in the second half of the year.

Net interest income was $4.3 million in the second quarter and $8.7 million year-to-date compared to net interest expense of $1.0 million and $3.5 million, respectively, in the same periods last year. These improvements were principally due to the early retirement of the Company's $150 million 8 $^{5}/_{8}$% Senior Subordinated Notes in the third quarter of fiscal 1999 and the conversion into equity of the Company's $230 million in preferred securities in the first quarter of fiscal 1999. Interest earned on higher cash balances resulting from faster inventory turns and earnings over the past four quarters in excess of $270 million also contributed to the improvement.

The Company's effective income tax rate for the second quarter was 38.1%, compared to 38.5% for the same quarter a year ago and 38.3% year-to-date compared to 38.5% for the year-to-date period last

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year. The Company's effective tax rate is primarily impacted by the taxability of investment income and state income taxes. Management's revised estimate of the annual effective tax rate of 38.3% for fiscal 2000 reflects higher levels of tax-exempt interest income. This revised annual estimate resulted in an effective rate of 38.1% in the second quarter.

Financial Condition

Working capital of $666 million at August 28, 1999 improved from $578 million a year ago. Cash and cash equivalents decreased by only $18 million compared to one year ago even with the retirement of over $180 million in debt, the repurchase of $100 million of the Company's common stock and the investment in new stores, corporate facilities and other initiatives to grow the business. Cash and cash equivalents decreased by $312 million compared to February 27, 1999, primarily due to investment in new stores and corporate facilities and the repurchase of $98 million of the Company's common stock in the first half of fiscal 2000. Merchandise inventories increased by $120 million compared to the second quarter last year, or 10%, while the number of stores open at the end of the second quarter increased by 15% and sales increased by 23% as inventory turns continued to improve. The rolling twelve month inventory turns improved nearly one full turn to 7.0 times for the period ended August 28, 1999, compared to 6.1 times for the period ended August 29, 1998. The Company's net investment in inventory, inventory net of accounts payable, was $229 million at August 28, 1999, down from $308 million at August 29, 1998. Merchandise inventories increased by $241 million compared to February 27, 1999, largely due to seasonality and the net addition of 21 stores in the first six months of fiscal 2000. The Company's cash position and net investment in inventory are impacted by the timing of payments to vendors and can vary significantly. Receivables increased by $38 million as compared to a year ago and $46 million compared to last fiscal year-end primarily due to higher business volumes including amounts due from the ISP subsidy provider. Recoverable costs from developed properties increased by $42 million compared to last year primarily due to the development of new stores. Other assets and long-term liabilities both increased due to the Company's deferred compensation plan, established in fiscal 1999. Accounts payable increased as compared to a year ago and last fiscal year-end as a result of the higher business volume and increased inventory levels. Accruals for payroll related liabilities increased as compared to last year's second quarter consistent with an expanding employee base needed to support the Company's growth, but decreased versus the prior fiscal year-end due to the payment of fiscal 1999 bonuses. Other accrued liabilities increased compared to August 29, 1998, as a result of the overall higher levels of business activity.

Capital spending in the first six months of fiscal 2000 was $145 million compared to $31 million for the same period last year as the Company invested in the 22 stores opened during the first six months and the 23 additional stores slated to open in the third quarter of fiscal 2000. Additionally, the Company invested in expanding its corporate facilities to support the growth of the business, the most significant investment being the purchase of an additional office building to supplement the Company's existing corporate office. The Company also continued to invest in new systems and technology to better position the Company for continued growth and generate improvements in its existing business.

Management expects total capital spending for fiscal 2000 to be approximately $400 million, exclusive of amounts expected to be recovered through subsequent sales and leasebacks, related to the Company's 45 new stores and 13 remodeled, expanded or relocated stores in fiscal 2000. Capital spending for the current year also includes expenditures required to support he Company's plans to open 55 to 60 stores in fiscal 2001, as well as further expansion of the Company's corporate headquarters capacity. In addition, the Company continues to invest in information systems to support the development of its e-commerce business and to improve its Services division.

In October 1998, the Company's Board of Directors authorized the purchase of up to $100 million of the Company's common stock over a twelve month period. This repurchase program was completed in the second quarter of fiscal 2000 as the Company purchased a total of 1.8 million shares. In September 1999, the Board authorized the purchase of up to an additional $200 million of the Company's common stock.

In August 1999, the Company entered into an unsecured $100 million revolving credit facility, replacing the $220 million facility that was scheduled to mature in June 2000. The Company was able to reduce the size of the facility due to improved operating performance and better inventory management. In addition, the new facility makes certain financial covenants less restrictive thereby providing the Company with additional flexibility. The current facility is scheduled to mature in August 2002.

Management believes that funds from the expected results of operations, and available cash and cash equivalents will be sufficient to support the Company's anticipated expansion plans and strategic initiatives for the next year. The revolving credit facility and the Company's inventory financing program are also available for additional working capital needs or opportunities.

Year 2000 Readiness

The Company recognized the material nature of the business issues surrounding computer processing of dates into and beyond the year 2000 (Y2K) and began taking corrective action in 1997. The Company's actions to address Y2K issues began with the selection of a nationally recognized, experienced computer hardware and consulting firm to assist in both identifying and resolving these issues. The Company developed specific and detailed plans to correct Y2K issues and management believes the Company has essentially completed all of the activities within its control to ensure the Company's systems are Y2K compliant. The Company has funded both the capital and expensed elements of resolving Y2K issues through funds generated from operations.

The majority of the Company's business processing applications operate on mainframe computer systems. The Company has replaced and tested all of the existing computer code effected by Y2K issues and the Company's mainframe systems are fully functional in its current fiscal year 2000, which began February 28, 1999. This portion of the Company's plan was completed last fiscal year at a cost of approximately $9 million in outside professional fees.

The Company has completed efforts to identify non-mainframe computer system Y2K issues and other potential Y2K issues. These issues include the Company's communication systems and operating systems at and between the Company's retail locations and support facilities. This portion of the Company's plan was completed at a total cost of approximately $9 million, with the majority incurred in the current year.

The Company has replaced or installed certain non-mainframe computer hardware and software that addressed new business application needs, as well as Y2K issues. The timing was accelerated for certain projects to meet Y2K compliance. The only implementation activities remaining are final implementation of the systems that support the Company's Services division and the in-store register system. Testing for both systems is expected to be completed during the third quarter.

The Company has communicated with its business partners, including significant merchandise suppliers and service providers to assess their ability to support the Company's operations with respect to their individual Y2K issues. These issues include data exchange with the Company, as well as the business partners' ability to maintain their production and shipping processes. The issues that were identified as part of this assessment have been prioritized in order of significance to the Company's operations and corrective actions are being taken as appropriate. All assessments have been scored and rated according to the risk to the Company's business. Both the Company's business partners and the Company's Y2K technical team collaborated on the ratings. To date, all of the Company's business partners deemed to have a potential material impact on the Company's operations have been assessed. Action plans were developed for each business partner that posed a material risk to the Company's ongoing operations. Actions, which include working with existing vendors to maintain the supply chain, will be taken through the end of the calendar year to minimize these risks.

The Company has also documented and reviewed the key internal processes required to operate its business. Each process was examined to determine if systems or third-party Y2K failures could impact the Company's business operations. Contingency plans to deal with potential business disruptions caused by Y2K failures will be completed in the third quarter. To further prepare for possible disruptions, the Company has planned a series of century change preparation activities including the creation of a Y2K internal call center to centrally manage Y2K events and support remote operations.

The Company generally believes that the vendors that supply products to the Company for resale are responsible for the Y2K functionality of those products. However, should product failures occur, the Company may be required to address certain aspects of those failures such as handling product returns or repairs. Actions to address this risk is included in the Company's contingency plans.

While the Company believes that it is pursuing the appropriate course of action to ensure Y2K readiness, there can be no assurance that the objective will be achieved either internally or as it relates to its business partners. Also, the Company can provide no assurance regarding potential impact on consumer spending that may result from concerns regarding the Y2K functionality of products. For the Y2K issues which, if not timely resolved, could have a significant impact on the Company's operations, the Company is continuing to develop contingency plans to minimize the impact of failure to achieve Y2K compliance. The Company has also devoted significant attention to planning for what could be the result of the most adverse consequence of Y2K issues including infrastructure failure or failure of core internal process systems. Management believes that appropriate actions have been taken to minimize the financial impact to the Company.

Safe Harbor Provisions Under the Private Securities Litigation Reform Act of 1995 (the "1995 Act")

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements to encourage companies to provide prospective information about their companies. With the exception of historical information, the matters discussed in this Quarterly Report on Form 10-Q are forward-looking statements and may be identified by the use of words such as "believe," "expect," "anticipate," "plan," "estimate," "intend" and "potential." Such statements reflect the current view of the Company with respect to future events and are subject to certain risks, uncertainties and assumptions. A variety of factors could cause the Company's actual results to differ materially from the anticipated results expressed in such forward-looking statements, including, among other things, general economic conditions, product availability, sales volumes, profit margins, the Company's and its suppliers' Year 2000 readiness, and the impact of labor markets and new product introductions on the Company's overall profitability. Readers are encouraged to review the Company's Current Report on Form 8-K filed on May 15, 1998, that describes additional important factors that could cause actual results to differ materially from those contemplated by the statements made herein.

PART II—OTHER INFORMATION

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K:

		Method of Filing
a.	Exhibits:	
	10.1 Credit Agreement dated August 9, 1999	(2)
	27.1 Financial Data Schedule	(1)
b.	Reports on Form 8-K:	
	None.	

(1) Document is filed herewith.

(2) Exhibit so marked was filed with the Securities and Exchange Commission on October 12, 1999 as an exhibit to the Form 10-Q of Best Buy Co., Inc. and is incorporated herein by reference and made a part hereof.

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.

BEST BUY CO., INC.
(Registrant)

Date: March 17, 2000

By: /s/ ROBERT C. FOX

Robert C. Fox
Senior Vice President Finance & Treasurer

QuickLinks

ARTICLE 5

THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE PERIODS INDICATED AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL

STATEMENTS.

MULTIPLIER: 1,000

PERIOD TYPE	6 MOS	6 MOS
FISCAL YEAR END	FEB 26 2000	FEB 27 1999
PERIOD START	FEB 28 1999	MAR 01 1998
PERIOD END	AUG 28 1999	AUG 29 1998
CASH	473,444	491,632
SECURITIES	0	0
RECEIVABLES	178,492	140,714
ALLOWANCES	0	0
INVENTORY	1,287,646	1,167,966
CURRENT ASSETS	2,064,416	1,877,894
PP&E	876,106	608,331
DEPRECIATION	353,286	208,137
TOTAL ASSETS	2,628,183	2,226,669
CURRENT LIABILITIES	1,398,243	1,299,892
BONDS	25,690	35,295
PREFERRED MANDATORY	0	0
PREFERRED	0	0
COMMON	20,527	10,077
OTHER SE	1,113,980	827,367
TOTAL LIABILITY AND EQUITY	2,628,183	2,226,669
SALES	5,072,071	4,116,149
TOTAL REVENUES	5,072,071	4,116,149
CGS	4,079,549	3,361,220
TOTAL COSTS	4,079,549	3,361,220
OTHER EXPENSES	831,215	663,708
LOSS PROVISION	0	0
INTEREST EXPENSE	(8,689)	3,505
INCOME PRETAX	169,996	87,716
INCOME TAX	65,120	33,784
INCOME CONTINUING	104,876	53,932
DISCONTINUED	0	0
EXTRAORDINARY	0	0
CHANGES	0	0
NET INCOME	104,876	53,932
EPS BASIC	.51	.27
EPS DILUTED	.49	.26

End of Filing