SPORTSMAN'S WAREHOUSE HOLDINGS, INC.
Form 10-K
March 24, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended January 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 001-36401

SPORTSMAN’S WAREHOUSE HOLDINGS, INC.

(Exact name of Registrant as specified in its Charter)

Delaware	39-1975614
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

7035 South High Tech Drive	
Midvale, Utah	84047
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (801) 566-6681

Securities registered pursuant to Section 12(b) of the Act: Common Stock, Par Value $0.01 Per Share; Common stock traded on the NASDAQ stock market

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES ¨ NO x

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. YES ¨ NO x

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 x 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 x NO ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405) is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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 definition of "large accelerated filer", "accelerated filer", and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	¨	Accelerated filer	x
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 x

As of July 31, 2015, the last business day of the registrant's most recently completed second quarter, the aggregate market value of the voting and non-voting common equity held by non-affiliates of the Registrant, based on the closing price of the shares of common stock on The NASDAQ Stock Market on July 31, 2015, was $210,123,179. Shares held by each executive officer, director and by each person who owns 10% or more of the outstanding common stock have been excluded in that such persons may be deemed to be affiliates. The determination of affiliate status is not necessarily a conclusive determination for other purposes.

The number of shares of Registrant’s Common Stock outstanding as of March 24, 2016 was 42,004,368.

Portions of the Registrant’s Definitive Proxy Statement relating to the 2016 Annual Meeting of Shareholders, which will be filed with the Securities and Exchange Commission within 120 days after the end of the 2015 fiscal year, are incorporated by reference into Part III of this Report.

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References throughout this document to “Sportsman’s Warehouse,” “we,” “us,” and “our” refer to Sportsman’s Warehouse Holdings, Inc. and its subsidiaries, and references to “Holdings” refer to Sportsman’s Warehouse Holdings, Inc. excluding its subsidiaries.

STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K (this “10-K) contains statements that constitute forward-looking statements as that term is defined by the Private Securities Litigation Reform Act of 1995. These statements concern our business, operations and financial performance and condition as well as our plans, objectives and expectations for our business operations and financial performance and condition, which are subject to risks and uncertainties. All statements other than statements of historical fact included in this 10-K are forward-looking statements. These statements may include words such as “aim,” “anticipate,” “assume,” “believe,” “can have,” “could,” “due,” “estimate,” “expect,” “goal,” “intend,” “li “objective,” “plan,” “potential,” “positioned,” “predict,” “should,” “target,” “will,” “would” and other words and terms of simi in connection with any discussion of the timing or nature of future operating or financial performance or other events or trends. For example, all statements we make relating to our plans and objectives for future operations, growth or initiatives and strategies are forward-looking statements.

These forward-looking statements are based on current expectations, estimates, forecasts and projections about our business and the industry in which we operate and our management’s beliefs and assumptions. We derive many of our forward-looking statements from our own operating budgets and forecasts, which are based upon many detailed assumptions. While we believe that our assumptions are reasonable, we caution predicting the impact of known factors is very difficult, and we cannot anticipate all factors that could affect our actual results.

All of our forward-looking statements are subject to risks and uncertainties that may cause our actual results to differ materially from our expectations. Important factors that could cause actual results to differ materially from our expectations include, but are not limited to:

- our retail-based business model is impacted by general economic conditions and economic and financial uncertainties may cause a decline in consumer spending;
- our concentration of stores in the Western United States makes us susceptible to adverse conditions in this region, which could affect our sales and cause our operating results to suffer;
- we operate in a highly fragmented and competitive industry and may face increased competition;
- we may not be able to anticipate, identify and respond to changes in consumer demands, including regional preferences, in a timely manner;
- we may not be successful in operating our stores in any existing or new markets into which we expand; and
- current and future government regulations, in particular regulations relating to the sale of firearms and ammunition, may impact the demand for our products and our ability to conduct our business.

The above is not a complete list of factors or events that could cause actual results to differ from our expectations, and we cannot predict all of them. All written and oral forward-looking statements attributable to us, or persons acting on our behalf, are expressly qualified in their entirety by the cautionary statements disclosed under “Risk Factors,” “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and elsewhere in this 10-K, as such disclosures may be amended, supplemented or superseded from time to time by other reports we file with the Securities and Exchange Commission (the “SEC”), including subsequent Annual Reports on Form 10-K and Quarterly Reports on Form 10-Q, and public communications. You should evaluate all forward-looking statements made in this 10-K and otherwise in the context of these risks and uncertainties.

Potential investors and other readers are urged to consider these factors carefully in evaluating the forward-looking statements and are cautioned not to place undue reliance on any forward-looking statements we make. These forward-looking statements speak only as of the date of this 10-K and are not guarantees of future performance or developments and involve known and unknown risks, uncertainties and other factors that are in many cases beyond our control. Except as required by law, we undertake no obligation to update or revise any forward-looking statements publicly, whether as a result of new information, future developments or otherwise.

PART I

Item 1. Business.

Overview

Sportsman's Warehouse is a high-growth outdoor sporting goods retailer focused on meeting the everyday needs of the seasoned outdoor veteran, the first-time participant and every enthusiast in between. Our mission is to provide a one-stop shopping experience that equips our customers with the right hunting, shooting, fishing and camping gear to maximize their enjoyment of the outdoors. We strive to accomplish this goal by tailoring our broad and deep merchandise assortment to meet local conditions and demand, offering everyday low prices, providing friendly support from our knowledgeable, highly trained staff and offering extensive in-store events and educational programming. These core strategies help position Sportsman's Warehouse as the "local outdoor experts" and the preferred place to both shop and share outdoor-based experiences in the communities we serve. As a result, we are expanding our loyal customer base in existing markets and increasing our store footprint in new markets, which we believe will further drive our growth and profitability.

Sportsman's Warehouse was founded in 1986 as a single retail store in Midvale, Utah and has grown to 66 stores across 20 states. Today, we have the largest outdoor specialty store base in the Western United States and Alaska. Our stores range from 15,000 to 65,000 gross square feet, with an average size of approximately 44,000 gross square feet. Our store layout is adaptable to both standalone locations and strip centers. Based on publicly available information, we believe it is less capital-intensive for us to open new stores compared to our principal competitors because our "no frills" store layout requires less initial cash investment to build out and our stores generally require less square footage than the stores of our competitors. Together, these features enable us to effectively serve markets of multiple sizes, from Metropolitan Statistical Areas, or MSAs, with populations of less than 75,000 to major metropolitan areas with populations in excess of 1,000,000, while generating consistent four-wall Adjusted EBITDA margins and returns on invested capital across a range of store sales volumes. We may post information that is important to investors on our website from time to time. The information provided on our website is not part of this report and is, therefore, not incorporated herein by reference.

Our Competitive Strengths

We believe the following competitive strengths allow us to capitalize on the growth opportunity within the outdoor activities and sporting goods market:

Differentiated Shopping Experience for the Seasoned Outdoor Veteran, the First-Time Participant and Every Enthusiast in Between. We place great emphasis on creating an inviting and engaging store experience for customers of all experience levels. For the seasoned outdoor veteran, we offer a one-stop, convenient store layout that promotes "easy-in, easy-out" access to replenish supplies, learn about local conditions and test products. We also serve first-time participants and casual users who are interested in enjoying the outdoors but enter our store without a clear sense for what equipment they need for their chosen activity. Our highly trained employees, who often are outdoor enthusiasts themselves and users of the products we sell, engage and interact with our customers in order to educate them and equip them with the right gear. Our sales associates draw upon both formal vendor sales training as well as first-hand experiences from using our products in local conditions. This selling approach allows us to offer a broad range of products and to deliver a shopping experience centered on the customer's needs, which we believe results in increased customer loyalty, repeat visits and frequent referrals to other potential customers.

A customer's shopping experience in our stores is further enhanced by a variety of helpful in-store offerings and features, including the issuance of hunting and fishing licenses, local fishing reports, availability of Sportsman's News (our proprietary in-store newspaper), access to the Braggin' Board (where customers can post photos of their outdoor adventures), indoor test ranges for archery equipment and displays of customer-owned taxidermy. In addition, we host a variety of in-store programs (such as “ladies night”), contests (such as Bucks & Bulls, a free-to-enter, big-game trophy contest) and a wide range of instructional seminars, from turkey frying to firearm operation and safety. These programs are all designed to help our customers connect with the outdoors and build the skill sets necessary to maximize enjoyment of their chosen activities. As a result, we believe our stores often serve as gathering spots where local enthusiasts can share stories, product knowledge and advice on outdoor recreation activities, which both drives traffic and fosters customer loyalty.

Locally Relevant Merchandise Serving the Comprehensive Needs of Outdoor Enthusiasts at a Compelling Value. We offer our customers an extensive and carefully selected assortment of branded, high-quality outdoor products at competitive prices. We accomplish this in three principal ways:

- Locally Relevant Merchandise: We carry over 70,000 SKUs on average in each store, out of a pool of approximately 120,000 total SKUs. Each store's merchandise is tailored to meet local conditions and consumer demand, taking into account seasonal requirements, regional game and fishing species, geographic diversity, weather patterns and key demographic factors, so that our customers have the right product, at the right time, for the right location.
- Breadth and Mix of Product Assortment: Our merchandise strategy is designed to serve a variety of purchasing occasions, from big-ticket items to replenishment activity, as well as to meet the wide-ranging needs of customers from first-time participants to seasoned outdoor veterans. We pride ourselves on carrying an extensive selection of branded, "good, better and best" hard goods at everyday low prices, including a broad array of in-stock consumable items. Approximately 35.0% of our unit sales and 20.0% of our dollar sales during fiscal year 2015 were consumable goods, such as ammunition, bait, cleaning supplies, food, lures, propane and reloading supplies. We believe this pairing of product breadth and consumable goods appeals to a broad range of customers and drives both repeat traffic and increased average ticket value.
- Strong Vendor Relationships: We believe our vendors find our "brand-centric," high-service store concept to be unique among national specialty outdoor retailers. Our attractive store locations, consistent presentation of merchandise and thorough product training present a compelling opportunity for our vendors to offer their brands to local markets that historically have been served primarily by "mom & pop" retailers. As a result, we believe we are able to negotiate terms with our vendors that are similar to those offered to our principal competitors that are larger in size. We share the benefits of these strategic vendor relationships with our customers through better pricing and enhanced access to certain products that are limited in production.

Flexible and Adaptable Real Estate Strategy. We believe that our store model, combined with our rigorous site selection process, is uniquely customizable to address the needs of the different markets we serve. Our stores can vary in size from approximately 15,000 to 65,000 gross square feet. We have had success with leasing existing sites as well as constructing new build-to-suit sites. Our flexible store model permits us to serve both large metropolitan areas, like Phoenix, Arizona, and smaller MSAs, like Soldotna, Alaska, while generating consistent four-wall Adjusted EBITDA margins and returns on invested capital across a range of store sales volumes. In small- to medium-sized markets, we are often able to establish ourselves as a standalone destination for our customers; in larger markets, we have successfully leveraged existing infrastructure to open stores in shopping plazas near complementary retailers, drawing upon existing foot traffic. We believe our low-cost, flexible model allows us to access both large and small markets more economically than many of our peers.

We maintain a disciplined approach to new store development and perform comprehensive market research before selecting a new site, including partnering with specialized, third-party local real estate firms. We select sites based on criteria such as local demographics, traffic patterns, density of hunting and fishing license holders in the area, abundance of hunting and fishing game and outdoor recreation activities, store visibility and accessibility, purchase data from our existing customer database and availability of attractive lease terms. We have established productive relationships with well-regarded commercial real estate firms and believe that we are a sought-after tenant, given the strength of the Sportsman's Warehouse brand, the high volume of customers that visit our stores and our flexible approach to site locations. As a result, we continue to have access to desirable retail sites on attractive terms.

Low Cost Operating Structure with Attractive and Replicable Store Economics. We strive to maintain a lower operating cost structure than our principal competitors, which allows us to serve small- to medium-sized markets as well as larger MSAs. We achieve this by exercising tight control over store-level expenses, real estate costs and corporate overhead. In addition, our growing store base, efficient, localized marketing spend and "no frills" warehouse store layout help us maintain comparatively low operating costs and provide us with the opportunity to achieve four-wall Adjusted EBITDA margins of 10% or more for stores in most new markets. Our typical new store requires an average net investment of approximately $2.0 million, which includes store build-out (net of contributions from landlords) and pre-opening cash expenditures. In addition, we stock each new store with initial inventory at an average cost of approximately $2.4 million. We target a pre-tax return on invested capital within one year after opening of over 50% excluding initial inventory cost (or over 20% including initial inventory cost), although our historical returns have often exceeded these thresholds. As of the end of fiscal year 2015, all of our stores that had been open for more than twelve months were profitable and those stores had an average Adjusted EBITDA margin of 14.1%. We believe this low-cost, capital-efficient approach also allows us to successfully serve markets that are not well-suited for the more capital-intensive store models of our principal competitors. Approximately 59% of our markets currently lack another nationally recognized outdoor specialty retailer, which we believe is a result of these dynamics.

Significant New Store Growth Opportunity within Existing and New Markets. We operate 66 stores across 20 states, primarily in the Western United States and Alaska, with a presence in these markets that is nearly three times that of the next largest outdoor retailer. We believe our leadership position in the Western United States, combined with our existing scalable infrastructure, provides a strong foundation for continued expansion within our core markets. Over the longer term, we believe our distinct retail concept has the potential to expand to more than 300 locations throughout the United States based on research conducted for us by Buxton Company, an independent consumer research and analytics firm.

Passionate and Experienced Management Team with Proven Track Record. We are focused on delivering an unsurpassed shopping experience to anyone who enjoys the excitement of the outdoors. This passion and commitment is shared by team members throughout our entire organization, from senior management to the employees in our stores. Our senior management team has an average of 20 years of retail experience, with extensive capabilities across a broad range of disciplines, including merchandising, real estate, finance, compliance, store operations, supply chain management and information technology. We also pride ourselves on the long tenure of our more than 200 store managers and corporate employees, who have been with us for an average of approximately 9 years.

Our Growth Strategy

We are pursuing a number of strategies designed to continue our growth and strong financial performance, including:

Expanding Our Store Base. We believe that our compelling new store economics and our track record of opening successful new stores provide a strong foundation for continued growth through new store openings in existing, adjacent and new markets. Over the last three fiscal years, we have opened an average of seven stores per year, excluding acquired stores. We have opened two new stores to date in fiscal year 2016 and currently plan to open an additional nine new stores in the remainder of fiscal year 2016. For the next several years thereafter, we intend to grow our store base at a rate of greater than 10 percent annually and expect that most of our near-term growth will occur within the Western United States. Our longer-term plans include expanding our store base to serve the outdoor needs of enthusiasts in markets across the United States. We believe our existing infrastructure, including distribution, information technology, loss prevention and employee training, is capable of sustaining 100 or more stores without significant additional capital investment.

Increasing Same Store Sales Growth. We are committed to increasing same store sales through a number of ongoing and new initiatives, including: expansion of our clothing offerings and private label program (such as our recently introduced proprietary Rustic Ridge™ and Killik™ clothing lines), our loyalty program, the implementation of kiosks and mobile point-of-sale in our stores and expansion of our “store-within-a-store” programs with major brands such as Carhartt, Columbia Sportswear and Under Armour. Each of these initiatives is designed to foster additional shopping convenience, add deeper merchandise selection and provide more product information to the customer. We believe these initiatives will drive additional traffic, improve conversion and increase average ticket value.

Continuing to Enhance Our Operating Margins. We believe that our planned expansion of our store base and growth in same store sales will result in improved Adjusted EBITDA margins as we take advantage of economies of scale in product sourcing and leverage our existing infrastructure, supply chain, corporate overhead and other fixed costs. Furthermore, we expect to increase our gross profit margin by expanding product offerings in our private label program, including our recently introduced proprietary Rustic Ridge™ and Killik™ clothing lines, and continuing marketing initiatives in our higher-margin clothing and footwear departments.

Growing the Sportsman’s Warehouse Brand. We are committed to supporting our stores, product offerings and brand through a variety of marketing programs, private label offerings and corporate partnerships. Our marketing and promotional strategy includes coordinated print, digital and social media platforms. In-store, we offer a wide range of outdoor-themed activities and seminars, from turkey frying to firearm operation and safety. In addition, we sponsor community outreach and charity programs to more broadly connect with our local communities with the aim of promoting our brand and educating consumers. Finally, we are committed to local chapters of national, regional and local wildlife federations and other outdoor-focused organizations, such as Ducks Unlimited and the Rocky Mountain Elk Foundation. Many of our store managers and employees serve in senior positions in these organizations, which further strengthens our place as leaders in the local outdoor community. We believe all of these programs promote our mission of engaging with our customers and serving outdoor enthusiasts.

Our Stores

We operate 66 stores across 20 states. Most of our stores are located in power, neighborhood and lifestyle centers. Power centers are large, unenclosed shopping centers that are usually anchored by three or more national supercenters, such as Target, Wal-Mart and Costco. Neighborhood centers are shopping centers anchored by a supermarket or drugstore that provide convenience goods and services to a neighborhood. Lifestyle centers are shopping centers that combine the traditional functions of a shopping mall with leisure amenities such as pedestrian friendly areas, open air seating and inviting meeting spaces. We also operate several single-unit, stand-alone locations. Our stores average approximately 44,000 gross square feet.

The following table lists the location by state of our 66 stores open as of March 24, 2016:

	Number of Stores		Number of Stores
Utah	8	New Mexico	2
Washington	8	Wyoming	2
Oregon	7	Iowa	1
Idaho	6	Kentucky	1
Arizona	5	Louisiana	1
California	5	Mississippi	1
Colorado	5	North Dakota	1
Alaska	4	South Carolina	1
Montana	3	Tennessee	1
Nevada	3	Virginia	1

Store Design and Layout

We present our broad and deep array of products in a convenient and engaging atmosphere to meet the everyday needs of all outdoor enthusiasts, from the seasoned veteran to the first-time participant. We maintain a consistent floor layout across our store base that we believe promotes an “easy-in, easy-out” shopping experience. All of our stores feature wide aisles, high ceilings, visible signage and central checkouts with multiple registers. Sportsman’s Warehouse stores, true to their name, are designed in a “no frills” warehouse format that welcomes customers directly from or on the way to an outdoor activity. All of our stores also feature “store-within-a-store” concepts for certain popular brand partners, such as Carhartt, Columbia Sportswear and Under Armour, through which we dedicate a portion of our floor space to these brands to help increase visibility and drive additional sales. The diagram below demonstrates our typical store layout.

Our stores include locally relevant features such as a large fishing board at the entrance that displays current fishing conditions in local lakes and rivers with coordinating gear in end-cap displays in the fishing aisles. We actively engage our customers through in-store features such as the Braggin’ Board, various contests (such as Bucks & Bulls and Fish Alaska), and customer-owned taxidermy displays on the walls. We also host in-store programs such as “ladies night” and a wide range of instructional seminars, from Dutch oven cooking to choosing the right binocular. Annually, we organize approximately 3,000 programs across our stores for the benefit of our customers. We believe these programs help us connect with the communities in which we operate and encourage first time participants to build the skills necessary to become outdoor enthusiasts and loyal customers.

Expansion Opportunities and Site Selection

We have developed a rigorous and flexible process for site selection. We select sites for new store openings based on criteria such as local demographics, traffic patterns, density of hunting and fishing license holders in the area, abundance of hunting and fishing game and outdoor recreation activities, store visibility and accessibility, purchase data from our existing customer database and availability of attractive lease terms. Our store model is adaptable to markets of multiple sizes, from MSAs with populations of less than 75,000 to major metropolitan areas with populations in excess of 1,000,000. We have been successful both in remodeling existing buildings and in constructing new build-to-suit locations.

Our store model is designed to be profitable in a variety of real estate venues, including power, neighborhood and lifestyle centers as well as single-unit, stand-alone locations. In small- to medium-sized markets, we generally seek anchor locations within high-traffic, easily accessible shopping centers. In larger metropolitan areas, we generally seek locations in retail areas with major discount retailers (such as Wal-Mart), wholesale retailers (such as Costco), other specialty hardline retailers (such as The Home Depot) or supermarkets. As we continue to expand our store base, we believe that small- to medium-sized markets offer a significant opportunity. In these markets, we believe our store size, which is smaller than many of our national competitors but larger than many independent retailers, enables us to find convenient, easily accessible store locations while still offering the broad and deep selection of merchandise that our customers desire. In addition, our store format and size allow us to open multiple stores in local areas within major MSAs, which gives our customers convenient, easy access to our products without having to travel long distances.

Members of our real estate team spend considerable time evaluating prospective sites before bringing a proposal to our real estate committee. Our real estate committee, which is comprised of senior management including our Chief Executive Officer, Chief Financial Officer and Senior Vice President of Stores, approves all prospective locations before a lease is signed.

We believe there is a significant opportunity to expand our store base in the United States. Based on research conducted for us by Buxton Company, we believe that we can grow our store base from 66 locations to more than 300 locations in the United States.

We opened nine new stores in fiscal year 2015. We have opened two new stores to date in fiscal year 2016 and currently plan to open an additional nine new stores in the remainder of fiscal year 2016. For the next several years thereafter, we intend to grow our store base at a rate of greater than 10 percent annually. Our new store openings are planned in existing, adjacent and new markets.

Our new store growth plan is supported by our target new unit economics, which we believe to be compelling. A typical store location ranges in size from 30,000 to 50,000 gross square feet. Our net investment to open a new store is approximately $2.0 million, consisting of pre-opening expenses and capital investments, net of tenant allowances. In addition, we stock each new store with initial inventory at an average cost of approximately $2.4 million. For the first twelve month period after opening a new store, we target net sales of $8.0 million to $11.0 million, a four-wall Adjusted EBITDA margin of more than 10% and a pre-tax return on invested capital of over 50% excluding initial inventory cost (or over 20% including initial inventory cost). Our new stores typically reach a mature sales growth rate within three to four years after opening, with net sales increasing approximately 25% in the aggregate during this time period. For the 20 stores opened since 2010 that have been open for a full twelve months, we achieved an average four-wall Adjusted EBITDA margin of 14.1% and an average ROIC of 98.3% excluding initial inventory cost (and 34.2% including initial inventory cost) during the first twelve months of operations. In addition, we achieved an average pre-tax payback period of less than one year (excluding initial inventory cost) and expect to achieve an average pre-tax payback period of approximately 2.5 years (including initial inventory cost).

E-Commerce Platform and Digital Strategy

We believe our website is an extension of our brand and our retail stores. Our website, www.sportsmanswarehouse.com, serves as both a sales channel and a platform for marketing and product education, and allows us to engage more fully with the local outdoor community. Our website features a similar merchandise assortment as offered in our stores as well as certain products found exclusively online. Regulatory restrictions create certain structural barriers to the online sale of approximately 30% of our revenue, such as ammunition, certain cutlery, firearms, propane and reloading powder. As a result, this portion of our business is currently more protected from online-only retailers, such as Amazon.

We also provide our online customers with convenient multi-channel services. To ensure that our customers have access to our entire assortment of products available on the e-commerce website, our retail stores feature kiosks that allow customers to place orders for items that are available only on our website or that are out of stock or not regularly stocked. We view our kiosk offering as an important complement to our larger format stores, as well as a key differentiator and extension of our smaller format stores. Our in-store pickup offering allows customers to order products through our e-commerce website and pick up the products in our retail stores without incurring shipping costs. We believe our ship-to-store functionality is a valuable service offering to customers, as well as a means to generate additional foot traffic to our retail stores.

Our website also features an online version of our Braggin' Board, which complements our retail store Braggin' Board forum. In addition, our website features local area content, including fishing reports and event schedules, as well as online educational resources, including tips, advice and links to video demonstrations on our dedicated YouTube channel. In fiscal year 2014, we launched enhanced department and product pages, detailed buyer's guides, and additional instructional product videos. We have also rolled out our social media strategy through our Facebook page and Instagram feed. These platforms allow us to reach our customers more directly with targeted postings of advertisements and in-store events. We believe our online educational resources and community outreach drive traffic to our website and retail stores, while improving user engagement as shoppers move from single-purchase users to loyal customers. We provide online customer service support and fulfill all orders in-house through our distribution center. During fiscal year 2015, our e-commerce platform generated total sales of $7.7 million, or 1.1% of our total sales. Over the same period, our website received approximately 13.0 million visits, which we believe demonstrates our position as a leading resource for outdoor products and product education.

Our Products and Services

Merchandise Strategy

We offer a broad range of products at a variety of price points and carry a deep selection of branded merchandise from well-known manufacturers, such as Browning, Carhartt, Coleman, Columbia Sportswear, Federal Premium Ammunition, Honda, Johnson Outdoors, Remington, Shakespeare, Shimano, Smith & Wesson and Under Armour. To reinforce our convenient shopping experience, we offer our products at competitive, everyday low prices. We believe our competitive pricing strategy supports our strong value proposition, instills price confidence in both our customers and our sales associates and is a critical element of our competitive position.

We believe we offer a wider selection of hard goods than many of our principal competitors. We employ a "good, better, and best" merchandise strategy, with an emphasis on "better" products that meet the needs of customers of all experience levels. We strive to keep our merchandise mix fresh and exciting by continuously searching for new, innovative products and introducing them to our customers. Our hunting and shooting department, which is strategically located at the back of the store, is a key driver of store traffic and one of the reasons for our high frequency of customer visits. We carry a large array of consumable goods, which includes ammunition, bait, cleaning supplies, food, lures, propane and reloading supplies. During fiscal year 2015, sales of consumable goods accounted for approximately 35.0% of our unit sales and 20.0% of our dollar sales. We believe the sale of consumables and replenishment items drives repeat traffic, with approximately 66% of our customers visiting our stores seven or more times per year (according to our internal surveys). During such visits, our customers frequently browse and purchase other items, including additional gear and accessories.

We also carry a variety of private label offerings under the Rustic Ridge™, Killik™, Vital Impact™, Yukon Gold, Lost River and Sportsman's Warehouse brands. These products are designed and priced to complement our branded assortment, by offering our customers a quality alternative at all price points. We believe the clothing, footwear and camping categories present a compelling near-term opportunity to expand our private label offering. In order to address these segments, we recently introduced our proprietary Rustic Ridge™ and Killik™ clothing lines. During fiscal year 2015, private label offerings accounted for less than 3.0% of our total sales, compared to more than 20% for many of our sporting goods retail peers. We believe our private label products are an important opportunity to drive sales and increase margins alongside our branded merchandise.

In addition to outfitting our customers with the correct gear, we provide our customers with various in-store, value-added, technical support services. All of our stores offer full-service archery technician services, fishing-reel line winding, gun bore sighting and scope mounting, among other services. We also help first-time participants enjoy the outdoors responsibly by issuing hunting and fishing licenses. We believe the support services provided by our highly trained staff technicians differentiate us from our competitors and drive customer loyalty and repeat traffic to our stores.

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Products

Our stores are organized into six departments. The table below summarizes the key product lines and brands by department:

Department	Product Offerings
Camping	Backpacks, camp essentials, canoes and kayaks, coolers, outdoor cooking equipment, sleeping bags, tents and tools
Clothing	Camouflage, jackets, hats, outerwear, sportswear, technical gear and work wear
Fishing	Bait, electronics, fishing rods, flotation items, fly fishing, lines, lures, reels, tackle and small boats
Footwear	Hiking boots, socks, sport sandals, technical footwear, trail shoes, casual shoes, waders and work boots
Hunting and Shooting	Ammunition, archery items, ATV accessories, blinds and tree stands, decoys, firearms, reloading equipment and shooting gear
Optics, Electronics and Accessories	Gift items, GPS devices, knives, lighting, optics (e.g., binoculars) and two-way radios

Each department has buying and planning teams that are responsible for monitoring product availability from vendors and sales volume within the department and across all stores. We actively monitor the profitability of each product category within each department and adjust our assortment and selling space accordingly. This flexibility enables us to provide customers with more preferred product choices and to enhance the profit potential of each store.

Hunting and shooting has historically been the largest contributor to our sales. Hunting and shooting department products are generally sold at significantly higher price points than other merchandise but often have lower margins. Camping is our second largest department, and family-oriented camping equipment in particular continues to be a high growth product category. Although clothing sales decreased as a percentage of total sales during fiscal year 2015, overall clothing sales have grown as we have introduced new brands and styles, including our selections for women and children. We view clothing sales as an important opportunity, given this department’s high gross margins and appeal to a broad, growing demographic.

The following table shows our sales during the past three fiscal years presented by department:

	Fiscal Year Ended		
Department	January 30, 2016	January 31, 2015	February 1, 2014
Camping	14.2 %	13.5 %	12.1 %
Clothing	8.6	9.5	8.8
Fishing	9.6	9.5	8.8
Footwear	7.1	7.4	6.6
Hunting and Shooting	48.6	47.9	52.1
Optics, Electronics and Accessories	9.3	9.5	9.1
Other	2.6	2.7	2.5
Total	100.0 %	100.0 %	100.0 %

Camping. Camping represented approximately 14.2% of our net sales during fiscal year 2015. Our camping assortment addresses both the technical requirements of the heavy-use camper, including gear for long-duration or deep-woods excursions, as well as the needs of the casual camper. We offer a broad selection of tents and shelters for both multi-day back country use and weekend outings, sleeping bags for the most extreme conditions as well as the summer overnight trip, backpacks and backpacking gear, including camouflaged styles for hunting, generators for home and camp use, cooking and food preparation equipment, including stoves and extended-use coolers, as well as dehydrated foods. Our camping department also includes canoes, kayaks and a selection of recreational family camping equipment, including basic automotive accessories, camp chairs and canopies. Our camping department includes brands such as Alps Mountaineering, Camp Chef, Coleman, Honda, Teton Sports, and Yeti Coolers.

Clothing. Clothing represented approximately 8.6% of our net sales during fiscal year 2015 and includes camouflage, outerwear, sportswear, technical gear, work-wear, jackets and hats. We primarily offer well-known brands in our clothing department, such as Carhartt, Columbia, Kings Mountain Shadow, Sitka, and Under Armour. We also intend to grow our proprietary clothing lines, Rustic Ridge™ and Killik™. Our clothing selection offers technical performance capabilities for a variety of hunting activities, including upland game, waterfowl, archery, big game hunting, turkey hunting and shooting sports. Performance attributes include waterproofing, temperature control, scent control features and visual capabilities, such as blaze orange and camouflage in a wide range of patterns. Outerwear, particularly performance rainwear, is an important product category for customers who are fishing, hiking, hunting or marine enthusiasts. We furthermore complement our technical clothing with an assortment of casual clothing that fits our customers’ lifestyles, including a variety of branded graphic t-shirts, and private label motto t-shirts.

Fishing . Fishing represented approximately 9.6% of our net sales during fiscal year 2015 and includes products for fresh-water fishing, salt-water fishing, fly-fishing, ice-fishing and boating. Our broad assortment appeals to the beginning and weekend angler, as well as avid and tournament anglers. In addition to lures, rods and reels, our fishing assortment features a wide selection of products in tackle management and organization, electronics, fly-fishing, ice-fishing and marine accessories sub-categories. We also provide fishing-reel line winding services in all of our stores and live bait in most of our stores. We offer products for boat care and maintenance, as well as safety equipment and aquatic products such as float tubes and pontoons. All of our stores also sell fishing licenses. Our fishing department includes brands such as Johnson Outdoors, Normark, Plano, Pure Fishing, Rivers Wild Flies, and Shimano.

Footwear . Footwear represented approximately 7.1% of our net sales during fiscal year 2015 and includes work boots, technical footwear, hiking boots, trail shoes, socks, sport sandals and waders. As with clothing, our footwear selection offers a variety of technical performance capabilities, such as different levels of support and types of tread, waterproofing, temperature control and visual attributes. Our footwear department includes brands such as Danner, Keen, Merrell, Red Wing, and Under Armour.

Hunting and Shooting. Hunting and shooting is our largest merchandise department, representing approximately 48.6% of our net sales during fiscal year 2015. Products such as ammunition, cleaning supplies, firearms and reloading selections are typically key drivers of traffic in our stores. Our hunting and shooting merchandise assortment provides equipment, accessories and consumable supplies for virtually every type of hunting and shooting sport. A backroom shop staffed with technicians allows us to support our hunting assortments for the benefit of the hunter, shooter, and archery enthusiast.

Our merchandise selection includes a wide variety of firearms designed for hunting, shooting sports and home and personal defense, including air guns, black powder muzzle loaders, handguns, rifles and shotguns. We carry a wide selection of ammunition, archery equipment, dog training products, hunting equipment, reloading equipment and shooting accessories. Our hunting and shooting department includes brands such as Federal Premium Ammunition, Hornady, Remington Arms, Ruger, Smith & Wesson, and Winchester.

Optics, Electronics and Accessories. Our optics, electronics and accessories department represented approximately 9.3% of our net sales during fiscal year 2015. This department supplements our other equipment departments with complementary products, such as optics (including binoculars, spotting scopes and rangefinders), GPS devices and other navigation gear, GoPro video cameras, two-way radios, specialized and basic cutlery and tools, including hunting and other knives, lighting, bear spray and other accessories. Our optics, electronics and accessories department includes brands such as Garmin, Leica, Nikon, Swarovski Optik and Vortex Optics.

Other. Our other department represented approximately 2.6% of our net sales during fiscal year 2015 and includes hunting and fishing licenses, background checks and miscellaneous services.

Loyalty Programs

We launched a loyalty program in the fall of 2013, through which our consumers are able to earn “points” towards Sportsman’s Warehouse gift cards on most of their purchases. The program is free to join and accepted through all channels for both purchases and the use of redemption cards. As of January 30, 2016, we had approximately 850,000 participants in our loyalty program.

Customers may obtain a loyalty program card when making a purchase in-store or online. After obtaining a card, the customer must register on our website in order to redeem loyalty rewards. Customers earn one point for each dollar spent, with the exception of certain items, such as gift cards and fish and game licenses. For every 100 points accumulated, the customer is entitled to a $1.00 credit in loyalty rewards, which may be redeemed by logging into our website to request a redemption card for any whole dollar amount (subject to the customer’s available point balance).

The redemption card is then mailed to the customer and operates as a gift card to be used for both in-store and online purchasing. The rewards points expire after 18 months of dormancy.

In addition, we began issuing the multi-use Sportsman's Warehouse Rewards VISA Platinum credit card in 2006 through US Bank. US Bank extends credit directly to cardholders and provides all servicing for the credit card accounts, funds the rewards and bears all credit and fraud losses. This card allows customers to earn points whenever and wherever they use their card. Customers may redeem earned points for products and services just as they would redeem loyalty card points.

Sourcing and Distribution

Sourcing

We maintain central purchasing, replenishment and distribution functions to manage inventory planning, allocate merchandise to stores and oversee the replenishment of basic merchandise to the distribution center. We have no long-term purchase commitments. During fiscal year 2015, we purchased merchandise from approximately 1,500 vendors with no vendor accounting for more than approximately 6% of total merchandise purchased. We have established long-standing, continuous relationships with our largest vendors.

Our sourcing organization is currently managed by our merchant team in our corporate headquarters. We also have field merchants that coordinate certain merchandising functions at the store level to provide a more localized merchandising model. To ensure that our product offerings are tailored to local market conditions and demand, our merchant teams regularly meet one-on-one with our vendors, and attend trade shows, review trade periodicals and evaluate merchandise offered by other retail and online merchants. We also frequently gather feedback and new product reviews from our store management and employees, as well as from reviews submitted by our customers. We believe this feedback is valuable to our vendor-partners and improves our access to new models and technologies.

Distribution and Fulfillment

We distribute all of our merchandise from our efficient 507,000 square foot distribution center in Salt Lake City, Utah. We opened this facility in July 2013, more than doubling the available space from our prior facility, in order to accommodate our growing store base and e-commerce platform. The distribution center supports replenishment for all 66 stores and manages the fulfillment of direct-to-consumer e-commerce orders. We use common carriers for replenishment of our retail stores. We ship merchandise to our e-commerce customers via courier service. An experienced distribution management team leads a staff of 250 distribution center employees at peak inventory levels heading into the fourth quarter.

The distribution center has scalable systems and processes that we believe can accommodate continued new store growth to exceed 100 stores. We use the HighJump warehouse management system to manage all activities. The system is highly adaptable and can be easily changed to accommodate new business requirements. For example, in 2010, we implemented a new picking process that allows e-commerce orders to be released without impacting the existing replenishment operations of the distribution center. Additionally, we have developed customized order packing and shipping processes to handle the specific requirements of the e-commerce business. We have the capability to both case pick and item pick, which is designed to ensure that our stores have sufficient quantities of product while also allowing us to maintain in inventory slow moving but necessary items. This balance allows us to stock the right products at the necessary locations, all at the right time and in the correct quantity.

Marketing and Advertising

We believe, based on internal surveys, that the majority of our customers are male, between the ages of 35 and 65, and have an annual household income between $40,000 and $100,000. We also actively market to women and children and have expanded our product offerings of women’s and children’s outerwear, clothing and footwear to address rising participation rates in hunting and shooting sports, as well as overall outdoor activity.

Our primary marketing efforts are focused on driving additional consumers to the stores and increasing the frequency and profitability of visits by customers of all types. We employ a two-pronged marketing approach:

- regional advertising programs; and
- local grass roots efforts to build brand awareness and customer loyalty.

Our regional advertising programs emphasize seasonal requirements for hunting, fishing and camping in our various store geographies. Our advertising medium is typically newspaper inserts (primarily multi-page color inserts during key shopping periods such as the Christmas season and Father’s Day), supplemented with modest amounts of direct mail, seasonal use of local and national television ads and a variety of out-of-home media buys. We proactively modify the timing and content of our message to match local and regional preferences, changing seasons, weather patterns and topography of a given region. In addition, the use of co-op funding with select vendors to supplement our out-of-pocket media expenses allows us to improve brand exposure through various advertising vehicles, while partnering with national brands in relevant media channels. This program also reinforces the general consumer’s impression of Sportsman’s Warehouse as a preferred retailer for those brands. Finally, we sponsor regional and national television programming, including sponsoring the Ultimate Bush Pilots, Angler’s Channel, Fishful Thinking, Hooked on Utah and RAM Outdoors. Our total media expenses for fiscal year 2015 were approximately $8.0 million, excluding co-op reimbursement of $1.4 million.

The second prong of our marketing effort is the time and resources devoted to fostering grass roots relationships in the local community. Each Sportsman's Warehouse store employs a variety of outreach tools to build local awareness. One key component to a successful store is hosting events throughout the year, targeting a variety of end user customer profiles (such as hunters, campers, anglers, women and children). In total, our store base hosts or facilitates approximately 3,000 in-store and offsite seminars and events per year, such as "ladies night," Eastman's Deer Tour, Waterfowl Weekend, Conservation Days contest and Bucks & Bulls. We are also active in supporting a variety of conservation groups, such as Ducks Unlimited, Rocky Mountain Elk Foundation, Mule Deer Foundation and the National Wild Turkey Federation, both at the corporate level and through store employee local memberships and participation. Company representatives attend more than 500 events annually in the aggregate, both to provide support for these organizations and to solidify ties between their members and the Sportsman's brand. Furthermore, we believe that the Sportsman's News newspaper, offered in-store, provides a unique point of contact with our customers by offering outdoor stories, product reviews, how-to articles and new product introductions to keep all of our customers up to date on the latest trends and technology. Finally, such grass roots campaigns enable us to reduce our initial marketing spend in connection with new store openings. We believe that these initiatives are highly cost-effective tools to create brand awareness and engender a loyal community of local customers, as well as a key differentiator versus other national retailers.

Hiring, Training and Motivating our Employees

We believe that the recruitment, training and knowledge of our employees and the consistency and quality of the service they deliver are central to our success. We emphasize deep product knowledge for store managers and sales associates at both the hiring and training stages. We hire most of our sales associates for a specific department or product category. As part of the interview process, we test each prospective employee for knowledge specific to the department or category in which he or she is applying to work. All of our managers and sales associates undergo focused sales training, consisting of both sales techniques and specialized product instruction, both immediately upon hiring (approximately 20 hours) and continuing throughout their career (approximately 16 hours annually). In addition, our sales associates receive loss prevention instruction and departmental training upon hiring. For example, in our hunting department, all employees receive an additional nine hours of training on ATF and company policies initially upon hire, with continuing education throughout the year. Our store managers complete two to six months of on-the-job training at another store with an existing district manager, as part of which they receive approximately 80 hours of dedicated managerial training and instruction. Our department heads receive extensive online training as well as on-site instruction, totaling approximately 40 hours. As a result of these programs, our employees are highly trained to provide friendly and non-intimidating education, guidance and support to address our customers' needs.

Our employees are often outdoor enthusiasts themselves, participating in outdoor activities alongside our customers in the local community. Our employees spend approximately 17% of their gross wages in-store, underscoring their passion for both our company and the outdoor lifestyle. We believe this high level of participation and employee store patronage is unique among our competitors in this industry and enhances our differentiated shopping experience.

One of our unique assets is a specially designed training room (our "blue room") located at our headquarters. Our blue room is used frequently for firm-wide training programs and by vendors to stage training demonstrations for new products. Blue room sessions are broadcast real-time in high definition to each store location and are recorded for future viewing. Vendor training is especially interactive, permitting vendor representatives to present a uniform message simultaneously to all employees, while allowing managers and sales staff in individual stores to ask questions of the vendors and provide real-time feedback on products. This system decreases the vendor's promotion and education costs and provides more meaningful training to our employees. Blue room training sessions are particularly important for technical products, especially those with numerous features and a high unit price, because they enable our sales associates to better educate customers and provide additional assurance that a given product fits the customer's needs. Given its utility as a cost-effective sales tool, our blue room is reserved well in advance by vendors. Our training program has been a critical factor in increasing conversion, which has led to average ticket growth of approximately 9% since the end of fiscal year 2010.

Information Technology

Business critical information technology, or IT, systems include our supply chain systems, merchandise system, point-of-sale (POS) system, warehouse management system, e-commerce system, loss prevention system and financial and payroll systems. Our IT infrastructure is robustly designed to be able to access real-time data from any store or channel. The network infrastructure allows us to quickly and cost effectively add new stores to the wide area network, or WAN. The private WAN is built on a CenturyLink (formerly Qwest) backbone with all of its resources and support. Additionally, we have implemented a redundant wireless WAN on Verizon’s infrastructure. Each Sportsman’s location is equipped with a backup power generator. All key systems will continue to run in the event of a power or network outage. All data is backed up daily from one storage array to another storage array.

We have implemented what we believe to be best-of-class software for all of our major business critical systems. Key operating systems include Oracle Applications for ERP, Oracle ATG for our e-commerce channel, Demandware's (formally Tomax's) Retail.net and JPOS for in-store functionality and HighJump for WMS. Our physical infrastructure is also built on products from best-in-class vendors Cisco, Dell, Oracle Sun and VMWare. Originally designed with the goal of being able to run a significantly larger retail business, our IT systems are scalable to support our growth.

The retail stores and the distribution center have loss prevention employees who monitor an average of 60 cameras at each store and 200 at the distribution center. These cameras are connected to digital video recorders (DVR) that record at least 30 days of video. Cameras are monitored locally during store hours. In addition, all cameras are monitored centrally at our headquarters in our dedicated surveillance room, which has capacity to monitor over 120 stores. This room is staffed continuously and provides off-hours monitoring and backup for all stores. Digital recorded video can be searched by pixel movement, which can quickly identify any loss prevention issue. Our sophisticated systems are a key factor in our shrink rates of less than 1% and an important component of our comprehensive compliance program.

We furthermore have incorporated enhanced reporting tools that have allowed for more comprehensive monitoring of business performance, which has been critical to management's ability to drive strong store level performance. Management has access to a reporting dashboard that shows key performance indicators, or KPIs, on a company, store, department and category level. KPIs include sales, margin, budget, conversions, payroll, shrinkage and average order value all on a daily, weekly, monthly and yearly basis. All KPIs are compared to comparable prior year periods. District, store and department managers have access to the data relevant to their area of responsibility. Real-time, up to the second, sales data is available on demand. The system allows for custom-created reports as required.

Intellectual Property

Sportsman's Warehouse®, Sportsman's Warehouse America's Premier Outfitter®, Lost Creek®, LC Lost Creek Fishing Gear and Accessories®, Rustic Ridge™, Killik™, K Killik & Design™, LC & Design™, and Vital Impact™ are among our service marks or trademarks registered with the United States Patent and Trademark Office. We also have a pending trademark application for Yukon Gold. In addition, we own several other registered and unregistered trademarks and service marks involving advertising slogans and other names and phrases used in our business. We also own numerous domain names, including www.sportsmanswarehouse.com, among others. The information on, or that can be accessed through, our websites is not a part of this filing.

We believe that our trademarks are valid and valuable and intend to maintain our trademarks and any related registrations. We do not know of any material pending claims of infringement or other challenges to our right to use our marks in the United States or elsewhere. We have no franchises or other concessions that are material to our operations.

Our Market and Competition

Our Market

We compete in the large, growing and fragmented outdoor activities and sporting goods market, which we believe is currently underserved by full-line multi-activity retailers. We believe, based on reports by the National Sporting Goods Association, or NSGA, and other industry sources, that U.S. outdoor activities and sporting goods retail sales totaled over $50 billion in 2013. The U.S. outdoor activities and sporting goods sector is comprised of three primary categories—equipment, clothing and footwear—with each category containing distinct product sets to support a variety of activities, including hunting, fishing, camping and shooting, as well as other sporting goods activities.

We believe growth in the U.S. outdoor activities and sporting goods market is driven by several key trends, including: an expanding demographic focused on healthy and active lifestyles; successful new product introductions centered around enhancing performance and enjoyment while participating in sporting and outdoor activities; and the resilience of consumer demand for purchases in these categories versus other discretionary categories. We believe these factors will continue to foster growth in the outdoor activities and sporting goods market in the future.

Within the retail sporting goods sector, we operate primarily in the outdoor equipment, clothing and footwear segment, which includes hunting and shooting, fishing, camping and boating. This segment is growing at a faster rate than the sporting goods industry at large. The 2011 U.S. Fish and Wildlife national survey, published once every five years, found that hunting and shooting and fishing participation increased 9% and 11%, respectively, for Americans aged 16 and older from 2006 to 2011. This survey also found that fishing participation among women increased by 17% over the same time period.

A 2015 NSGA report indicated that, from 2013 to 2014, there was a 7% increase in hunting with firearms participation, a 7% increase in target shooting (live ammunition) participation, a 9% increase in fishing (fresh water) participation, a 9% increase in female participation in target shooing (live ammo), and an 8% increase in female participation in fishing (fresh water) in the United States.

Furthermore, we believe that specialty retailers have generated additional sales volume by expanding their presence, especially in smaller communities, which has increased customers' access to products that formerly were less available. The nature of the outdoor activities to which we cater requires recurring purchases throughout the year, resulting in high rates of conversion among customers. For example, active anglers typically purchase various fishing tackle throughout the year based on seasons and changing conditions. Hunting with firearms typically is accompanied by recurring purchases of ammunition and cleaning supplies throughout the year and multiple firearm styles for different hunted game.

Competition

We believe that the principal competitive factors in our industry are breadth and depth of product selection, including locally relevant offerings, value pricing, convenient locations, technical services and customer service. A few of our competitors have a larger number of stores, and some of them have a greater market presence, name recognition and financial, distribution, marketing and other resources than we have. We believe that we compete effectively with our competitors with our distinctive branded selection and superior customer service, as well as our commitment to understanding and providing merchandise that is relevant to our targeted customer base. We cater to the outdoor enthusiast and believe that we have both an in-depth knowledge of the technical outdoor customer and a "grab and go" store environment that is uniquely conducive to their need for value and convenience. We believe that our flexible box size, combined with our low-cost, high-service model, also allows us to enter into and serve smaller markets that our larger competitors cannot penetrate as effectively. Finally, certain barriers, including legal restrictions, exist on the sale of our product offerings that comprise approximately 30% of our revenue, such as ammunition, certain cutlery, firearms, propane and reloading powder, create a structural barrier to competition from many online retailers, such as Amazon.

Our principal competitors include the following:

- independent, local specialty stores, often referred to as "mom & pops";
- other specialty retailers that compete with us across a significant portion of our merchandising categories through retail store, catalog or e-commerce businesses, such as Bass Pro Shops, Cabela's and Gander Mountain;
- large-format sporting goods stores and chains, such as Academy Sports + Outdoors and Dick's Sporting Goods; and
- mass merchandisers, warehouse clubs, discount stores, department stores and online retailers, such as Amazon, Target and Wal-Mart.

Independent, Local Specialty Stores. These stores generally range in size from approximately 2,000 to 10,000 square feet, and typically focus on one or two specific product categories, such as hunting, fishing or camping, and usually lack a broad selection of product.

Other Specialty Retailers. Some of the other specialty retailers that compete with us across a significant portion of our merchandising categories are large-format retailers that generally range in size from 40,000 to 250,000 square feet. These retailers seek to offer a broad selection of merchandise focused on hunting, fishing, camping and other outdoor product categories. Some of these stores combine the characteristics of an outdoor retailer with outdoor entertainment and theme attractions. We believe that the number of these stores that can be supported in any single market area is limited because of their large size and significant per-store cost.

Other specialty retailers are smaller chains that typically focus on offering a broad selection of merchandise in one or more of the following product categories—hunting, fishing, camping or other outdoor product categories. We believe that these other outdoor-focused chains generally do not offer a similar depth and breadth of merchandise or specialized services in all of our product categories.

Large-Format Sporting Goods Stores And Chains. These stores generally range from 20,000 to 80,000 square feet and offer a broad selection of sporting goods merchandise covering a variety of sporting goods categories, including baseball, basketball, football and home gyms, as well as hunting, fishing and camping. However, we believe that the amount of space at these stores devoted to our outdoor product categories limits the extent of their offerings in these areas.

Mass Merchandisers, Warehouse Clubs, Discount Stores, Department Stores and Online Retailers. With respect to retailers in this category with physical stores, these stores generally range in size from approximately 50,000 to over 200,000 square feet and are primarily located in shopping centers, free-standing sites or regional malls. Hunting, fishing and camping merchandise and clothing represent a small portion of the stores' assortment, and of their total sales. We believe that less than 10% of our product offering, and less than 5% of our hunting and shooting product offering, overlap with these stores.

Over the past decade, specialty retailers, such as us, have gained market share of equipment sales at the expense of mass merchants, discount stores and independent retailers, or "mom & pop" shops, which we believe comprise approximately 65% of the market. In addition, while there are over 55,000 Type 01 Federal Firearms Licenses, or FFLs, in the United States today, only 4,400 are currently held by national or regional specialty stores. Since FFLs are issued at the store level, these statistics imply that the remaining 92% of the market is fragmented among mom & pop stores. We believe this fragmentation within the total addressable market presents an attractive opportunity for us to continue to expand our market share, as customers increasingly prefer a broad and appealing selection of merchandise, competitive prices, high levels of service and one-stop shopping convenience.

Seasonality

We experience moderate seasonal fluctuations in our net sales and operating results as a result of holiday spending and the opening of hunting seasons. While our sales are more level throughout the year than many retailers, our sales are still traditionally somewhat higher in the third and fourth fiscal quarters than in the other quarterly periods. On average over the last three fiscal years, we have generated 27.4% and 28.2% of our net sales in the third and fourth fiscal quarters, respectively, which includes the holiday selling season as well as the opening of the fall hunting season. However, Spring hunting, Father's Day and the availability of hunting and fishing throughout the year in many of our markets counterbalance this seasonality to a certain degree. For additional information, see Part II, Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operation."

Regulation and Compliance

Regulation and Legislation

We operate in highly regulated industries. There are a number of federal, state and local laws and regulations that affect our business. In every state in which we operate, we must obtain various licenses or permits in order to operate our business.

Because we sell firearms at all of our retail stores, we are subject to regulation by the Bureau of Alcohol, Tobacco, Firearms and Explosives, or the "ATF". Each store has a federal firearms license permitting the sale of firearms, and our distribution center has obtained a federal firearms license to store and distribute firearms. Certain states require a state license to sell firearms, and we have obtained these licenses for the states in which we operate that have such a requirement.

We must comply with federal, state and local laws and regulations, including the National Firearms Act of 1934, or NFA, the Gun Control Act of 1968, or GCA, the Arms Export Control Act of 1976 and Internal Revenue Code provisions applicable to the Firearms and Ammunition Excise Tax, all of which have been amended from time to time. The NFA and the GCA require our business to, among other things, maintain federal firearms licenses for our locations and perform a pre-transfer background check in connection with all firearms purchases. We perform this background check using either the FBI-managed National Instant Criminal Background Check System, or NICS, or a comparable state government-managed system that relies on NICS and any additional information collected by the state, a state point of contact. These background check systems either confirm that a transfer can be made, deny the transfer or require that the transfer be delayed for further review, and provide us with a transaction number for the proposed transfer. We are required to record the transaction number on an ATF Form 4473 and retain this form in our records for auditing purposes for 20 years for each approved transfer and five years for each denied or delayed transaction.

The federal categories of prohibited purchasers are the prevailing minimum for all states. States (and, in some cases, local governments) on occasion enact laws that further restrict permissible purchasers of firearms. We are also subject to numerous other federal, state and local laws and regulations regarding firearm sale procedures, record keeping, inspection and reporting, including adhering to minimum age restrictions regarding the purchase or possession of firearms or ammunition, residency requirements, applicable waiting periods, importation regulations and regulations pertaining to the shipment and transportation of firearms.

Over the past several years, bills have been introduced in the United States Congress that would restrict or prohibit the manufacture, transfer, importation or sale of certain calibers of handgun ammunition, impose a tax and import controls on bullets designed to penetrate bullet-proof vests, impose a special occupational tax and registration requirements on manufacturers of handgun ammunition and increase the tax on handgun ammunition in certain calibers. Recently, Congress has debated certain gun control measures that are supported by the current administration.

In September 2004, Congress declined to renew the Assault Weapons Ban of 1994, or AWB, which prohibited the manufacture of certain firearms defined as “assault weapons”; restricted the sale or possession of “assault weapons,” except those that were manufactured prior to the law’s enactment; and placed restrictions on the sale of new high capacity ammunition feeding devices. Various states and local jurisdictions, including Colorado and California (states in which we operate stores), have adopted their own versions of the AWB or high capacity ammunition feeding device restrictions, some of which restrictions apply to the products we sell in other states. If a statute similar to the AWB were to be enacted or re-enacted at the federal level, it would impact our ability to sell certain products. Additionally, state and local governments have proposed laws and regulations that, if enacted, would place additional restrictions on the manufacture, transfer, sale, purchase, possession and use of firearms, ammunition and shooting-related products. For example, several states, such as Colorado, Connecticut, Maryland, New Jersey, New York, and Washington have enacted laws and regulations that are more restrictive than federal laws and regulations that limit access to and sale of certain firearms. For example, Connecticut and New York impose mandatory screening of ammunition purchases; California and the District of Columbia have requirements for microstamping (that is, engraving the handgun’s serial number on each cartridge) of new handguns; and some states prohibit the sale of guns without internal or external locking mechanisms. Other state or local governmental entities may also explore similar legislative or regulatory initiatives that may further restrict the manufacture, sale, purchase, possession or use of firearms, ammunition and shooting-related products.

The Protection of Lawful Commerce in Arms Act, which became effective in October 2005, prohibits civil liability actions from being brought or continued in any federal or state court against federally licensed manufacturers, distributors, dealers or importers of firearms or ammunition for damages, punitive damages, injunctive or declaratory relief, abatement, restitution, fines, penalties or other relief resulting from the criminal or unlawful misuse of a qualified product by third parties. The legislation does not preclude traditional product liability actions.

We are also subject to a variety of federal, state and local laws and regulations relating to, among other things, protection of the environment, human health and safety, advertising, pricing, weights and measures, product safety, and other matters. Some of these laws affect or restrict the manner in which we can sell certain items, such as handguns, smokeless powder, black powder substitutes, ammunition, bows, knives and other products. State and local laws and regulations governing hunting, fishing, boating, ATVs and other outdoor activities and equipment can also affect our business. We believe that we are in substantial compliance with the terms of such laws and that we have no liabilities under such laws that we expect could have a material adverse effect on our business, results of operations or financial condition.

In addition, many of our imported products are subject to existing or potential duties, tariffs or quotas that may limit the quantity of products that we may import into the United States and other countries or impact the cost of such products. To date, quotas in the operation of our business have not restricted us, and customs duties have not comprised a material portion of the total cost of our products.

Our e-commerce business is subject to the Mail or Telephone Order Merchandise Rule and related regulations promulgated by the FTC which affect our catalog mail order operations. FTC regulations, in general, govern the solicitation of orders, the information provided to prospective customers, and the timeliness of shipments and refunds. In addition, the FTC has established guidelines for advertising and labeling many of the products we sell.

Compliance

We are routinely inspected by the ATF and various state agencies to ensure compliance with federal and local regulations. While we view such inspections as a starting point, we employ more thorough internal compliance inspections to help ensure we are in compliance with all applicable laws. Our compliance department conducts at least one on-site inspection of each store location annually. With the IT infrastructure systems we have in place, recall inspections can be done remotely.

We dedicate significant resources to ensure compliance with applicable federal, state and local regulations. Since we began operations in 1986, none of our federal firearm licenses have been revoked, and none of our ATF compliance inspections within the last ten years have resulted in a major violation.

We are also subject to a variety of state laws and regulations relating to, among other things, advertising and product restrictions. Some of these laws prohibit or limit the sale, in certain states and locations, of certain items, such as black powder firearms, ammunition, bows, knives, and similar products. Our compliance department administers various restriction codes and other software tools to prevent the sale of such jurisdictionally restricted items.

We have particular expertise in the California market and have passed several California Department of Justice, or CA DOJ, firearm audits with zero violations or only minor violations. The CA DOJ communicates with us for policy discussion, recognizing the strength of our compliance infrastructure.

Employees

As of February 29, 2016 we had approximately 4,200 total employees. Of our total employees, approximately 200 were based at our corporate headquarters in Midvale, Utah, approximately 250 were located at our distribution center, and approximately 3,750 were store employees. We had approximately 1,900 full-time employees and approximately 2,300 part-time employees, who are primarily store employees. None of our employees are represented by a labor union or are party to a collective bargaining agreement, and we have had no labor-related work stoppages. Our relationship with our employees is one of the keys to our success, and we believe that relationship is good.

Available Information

Our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to reports filed or furnished pursuant to Sections 13(a) and 15(d) of the Securities Exchange Act of 1934, as amended, or the Exchange Act are available on our web site at www.sportsmanswarehouse.com, free of charge, as soon as reasonably practicable after the electronic filing of these reports with, or furnishing of these reports to, the SEC. Any materials we file with the SEC are available at the SEC’s Public Reference Room at 100 F Street, NE, Washington, DC 20549. Additional information about the operation of the Public Reference Room can also be obtained by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains a web site at www.sec.gov that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, including us.

ITEM 1A. RISK FACTORS

Our business faces significant risks and uncertainties. Certain important factors may have a material adverse effect on our business prospects, financial condition and results of operations, and you should carefully consider them. Accordingly, in evaluating our business, we encourage you to consider the following discussion of risk factors, in its entirety, in addition to other information contained in or incorporated by reference into this 10-K and our other public filings with the SEC. Other events that we do not currently anticipate or that we currently deem immaterial may also affect our business, prospects, financial condition and results of operations.

Risks Related to Our Business

Our retail-based business model is impacted by general economic conditions in our markets, and ongoing economic and financial uncertainties may cause a decline in consumer spending that may adversely affect our business, operations, liquidity, financial results and stock price.

As a retail business that depends on consumer discretionary spending, we may be adversely affected if our customers reduce, delay or forego their purchases of our products as a result of continued job losses, bankruptcies, higher consumer debt and interest rates, higher energy and fuel costs, reduced access to credit, falling home prices, lower consumer confidence, uncertainty or changes in tax policies and tax rates and uncertainty due to potential national or international security concerns. Decreases in same store sales, customer traffic or average ticket sales negatively affect our financial performance, and a prolonged period of depressed consumer spending could have a material adverse effect on our business. Promotional activities, vendor incentives, and decreased demand for consumer products could affect profitability and margins. In addition, adverse economic conditions may result in an increase in our operating expenses due to, among other things, higher costs of labor, energy, equipment and facilities. Due to recent fluctuations in the U.S. economy, our sales, operating and financial results for a particular period are difficult to predict, making it difficult to forecast results to be expected in future periods. Any of the foregoing factors could have a material adverse effect on our business, results of operations and financial condition and could adversely affect our stock price.

Our concentration of stores in the Western United States makes us susceptible to adverse conditions in this region.

The majority of our stores are located in the Western United States, comprising Alaska, Arizona, California, Colorado, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington and Wyoming. As a result, our operations are more susceptible to regional factors than the operations of more geographically diversified competitors. These factors include regional economic and weather conditions, natural disasters, demographic and population changes and governmental regulations in the states in which we operate. Environmental changes and disease epidemics affecting fish or game populations in any concentrated region may also affect our sales. If a region with a concentration of our stores were to suffer an economic downturn or other adverse event, our operating results could suffer.

Competition in the outdoor activities and sporting goods market could reduce our net sales and profitability.

The outdoor activities and sporting goods market is highly fragmented and competitive. We compete directly or indirectly with the following types of companies:

- independent, local specialty stores, often referred to as "mom & pops";
- other specialty retailers that compete with us across a significant portion of our merchandising categories through retail store, catalog or e-commerce businesses, such as Bass Pro Shops, Cabela's and Gander Mountain;
- large-format sporting goods stores and chains, such as Academy Sports + Outdoors and Dick's Sporting Goods; and
- mass merchandisers, warehouse clubs, discount stores, department stores and online retailers, such as Amazon, Target and Wal-Mart.

A few of our competitors have a larger number of stores, and some of them have a greater market presence, name recognition and financial, distribution, marketing and other resources than we have. In addition, if our competitors reduce their prices, we may have to reduce our prices in order to compete, which could harm our margins. Furthermore, some of our competitors may build new stores in or near our existing locations. As a result of this competition, we may need to spend more on advertising and promotion. Some of our mass merchandising competitors, such as Wal-Mart, do not currently compete in many of the product lines we offer. However, if these competitors were to begin offering a broader array of competing products, or if any of the other factors listed above occurred, our net sales could be reduced or our costs could be increased, resulting in reduced profitability.

If we fail to anticipate changes in consumer demands, including regional preferences, in a timely manner, our operating results could suffer.

Our products appeal to consumers who regularly hunt, camp, fish and participate in various shooting sports. The preferences of these consumers cannot be predicted with certainty and are subject to change. In addition, due to different game and fishing species and varied weather conditions found in different markets, it is critical that our stores stock products appropriate for their markets. Our success depends on our ability to identify product trends in a variety of markets as well as to anticipate, gauge and quickly react to changing consumer demands in these markets. We usually must order merchandise well in advance of the applicable selling season. The extended lead times for many of our purchases may make it difficult for us to respond rapidly to new or changing product trends or changes in prices. If we misjudge either the market for our products or our customers' purchasing habits, our net sales may decline significantly and we may not have sufficient quantities of merchandise to satisfy customer demand or we may be required to mark down excess inventory, either of which would result in lower profit margins and harm our operating results.

Our expansion into new, unfamiliar markets presents increased risks that may prevent us from being profitable in these new markets.

We intend to expand by opening stores in new markets, which may include small- to medium-sized markets and which may not have existing national outdoor sports retailers. As a result, we may have less familiarity with local customer preferences and encounter difficulties in attracting customers due to a reduced level of customer familiarity with our brand. Other factors that may impact our ability to open stores in new markets and operate them profitably, many of which are beyond our control, include:

- our ability to identify suitable locations, including our ability to gather and assess demographic and marketing data to determine consumer demand for our products in the locations we select;
- our ability to negotiate favorable lease agreements;
- our ability to properly assess the profitability of potential new retail store locations;
- our ability to secure required governmental permits and approvals;
- our ability to hire and train skilled store operating personnel, especially management personnel;
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the availability of construction materials and labor and the absence of significant construction delays or cost overruns;

- our ability to provide a satisfactory mix of merchandise that is responsive to the needs of our customers living in the areas where new retail stores are built;
- our ability to supply new retail stores with inventory in a timely manner;
- our competitors building or leasing stores near our retail stores or in locations we have identified as targets for a new retail store;
- consumer demand for our products, particularly firearms and ammunition, which drives traffic to our retail stores;

- regional economic and other factors in the geographies in which we expand; and
- general economic and business conditions affecting consumer confidence and spending and the overall strength of our business.

Once we decide on a new market and find a suitable location, any delays in opening new stores could impact our financial results. It is possible that events, such as delays in the entitlements process or construction delays caused by permitting or licensing issues, material shortages, labor issues, weather delays or other acts of god, discovery of contaminants, accidents, deaths or injunctions, could delay planned new store openings beyond their expected dates or force us to abandon planned openings altogether. In addition, new retail stores typically generate lower operating margins because pre-opening expenses are expensed as they are incurred and because fixed costs, as a percentage of net sales, are higher. Furthermore, the substantial management time and resources which our retail store expansion strategy requires may result in disruption to our existing business operations, which may decrease our profitability.

As a result of the above factors, we cannot assure you that we will be successful in operating our stores in new markets on a profitable basis.

Our planned growth may strain our business infrastructure, which could adversely affect our operations and financial condition.

Over time, we expect to expand the size of our retail store network in new and existing markets. As we grow, we will face the risk that our existing resources and systems, including management resources, accounting and finance personnel and operating systems, may be inadequate to support our growth. We cannot assure you that we will be able to retain the personnel or make the changes in our systems that may be required to support our growth. Failure to secure these resources and implement these systems on a timely basis could have a material adverse effect on our operating results. In addition, hiring additional personnel and implementing changes and enhancements to our systems will require capital expenditures and other increased costs that could also have a material adverse impact on our operating results.

Our expansion in new markets may also create new distribution and merchandising challenges, including strain on our distribution facility, an increase in information to be processed by our management information systems and diversion of management attention from existing operations towards the opening of new stores and markets. To the extent that we are not able to meet these additional challenges, our sales could decrease and our operating expenses could increase.

Our ability to operate and expand our business and to respond to changing business and economic conditions will depend on the availability of adequate capital.

The operation of our business, the rate of our expansion and our ability to respond to changing business and economic conditions depend on the availability of adequate capital, which in turn depends on cash flow generated by our business and, if necessary, the availability of equity or debt capital. We will also need sufficient cash flow to meet our obligations under our existing debt agreements. We paid total cash interest on our credit facilities of $12.8 million, $16.4 million and $19.0 million in fiscal years 2015, 2014 and 2013, respectively, and our term loans require us to make quarterly principal payments of $0.4 million.

We are required to make mandatory prepayments based on any excess cash flows as defined in the term loan agreement. Due to our profitability during fiscal year 2015, we are required to make a mandatory prepayment of approximately $7.7 million by May 6, 2016, which will reduce the outstanding amount under the term loan.

The amount that we are able to borrow and have outstanding under our revolving credit facility at any given time is subject to a borrowing base calculation, which is a contractual calculation equal to roughly (1) the lesser of (a) 90% of the net orderly liquidation value of our eligible inventory, and (b) 75% of the lower of cost or market value of our eligible inventory, plus (2) 90% of the eligible accounts receivable, less certain reserves against outstanding gift cards, layaway deposits and amounts outstanding under commercial letters of credit, each term as defined in the credit agreement for the revolving credit facility. As a result, our ability to borrow is subject to certain risks and uncertainties, such as a deterioration in the quality of our inventory (which is the largest asset in our borrowing base), a decline in sales activity and the collection of our receivables, which could reduce the funds available to us under our revolving credit facility.

We cannot assure you that our cash flow from operations or cash available under our revolving credit facility will be sufficient to meet our needs. If we are unable to generate sufficient cash flows from operations in the future, and if availability under our revolving credit facility is not sufficient, we may have to obtain additional financing. If we obtain additional capital by issuing equity, the interests of our existing stockholders will be diluted. If we incur additional indebtedness, that indebtedness may contain significant financial and other covenants that may significantly restrict our operations. We cannot assure you that we could obtain refinancing or additional financing on favorable terms or at all.

Our revolving credit facility and term loans contain restrictive covenants that may impair our ability to access sufficient capital and operate our business.

Our revolving credit facility and term loans contain various provisions that limit our ability to, among other things:

- incur, create or assume certain indebtedness;
- create, incur or assume certain liens;
- make certain investments;
- make sales, transfers and dispositions of certain property;
- undergo certain fundamental changes, including certain mergers, liquidations and consolidations;
- purchase, hold or acquire certain investments; and
- declare or make certain dividends and distributions.

These covenants may affect our ability to operate and finance our business as we deem appropriate. If we are unable to meet our obligations as they become due or to comply with various financial covenants contained in the instruments governing our current or future indebtedness, this could constitute an event of default under the instruments governing our indebtedness.

If there were an event of default under the instruments governing our indebtedness, the holders of the affected indebtedness could declare all of that indebtedness immediately due and payable, which, in turn, could cause the acceleration of the maturity of all of our other indebtedness. We may not have sufficient funds available, or we may not have access to sufficient capital from other sources, to repay any accelerated debt. Even if we could obtain additional financing, the terms of the financing may not be favorable to us. In addition, substantially all of our assets are subject to liens securing our revolving credit facility and term loans. If amounts outstanding under the revolving credit facility or term loans were accelerated, our lenders could foreclose on these liens and we could lose substantially all of our assets. Any event of default under the instruments governing our indebtedness could have a material adverse effect on our business, financial condition and results of operations.

Our same store sales may fluctuate and may not be a meaningful indicator of future performance.

Our same store sales may vary from quarter to quarter, and an unanticipated decline in net sales or same store sales may cause the price of our common stock to fluctuate significantly. A number of factors have historically affected, and will continue to affect, our same store sales results, including:

- changes or anticipated changes to regulations related to some of the products we sell;
- consumer preferences, buying trends and overall economic trends;
- our ability to identify and respond effectively to local and regional trends and customer preferences;
- our ability to provide quality customer service that will increase our conversion of shoppers into paying customers;
- competition in the regional market of a store;
- atypical weather;
- changes in our product mix; and
- changes in pricing and average ticket sales.

Our operating results are subject to seasonal fluctuations.

We experience moderate seasonal fluctuations in our net sales and operating results. On average over the last three fiscal years, we have generated 27.4% and 28.2% of our annual net sales in the third and fourth fiscal quarters, respectively, which includes the holiday selling season as well as the opening of the fall hunting season. We incur additional expenses in the third and fourth fiscal quarters due to higher purchase volumes and increased staffing in our stores. If, for any reason, we miscalculate the demand for our products or our product mix during the third or fourth fiscal quarters, our sales in these quarters could decline, resulting in higher labor costs as a percentage of sales, lower margins and excess inventory, which could cause our annual operating results to suffer and our stock price to decline. Due to our seasonality, the possible adverse impact from other risks associated with our business, including atypical weather, consumer spending levels and general business conditions, is potentially greater if any such risks occur during our peak sales seasons.

We rely on a single distribution center for our business, and if there is a natural disaster or other serious disruption at such facility, we may be unable to deliver merchandise effectively to our stores or customers.

We rely on a single distribution center in Salt Lake City, Utah for our business. Any natural disaster or other serious disruption at such facility due to fire, tornado, earthquake, flood or any other cause could damage our on-site inventory or impair our ability to use such distribution center. While we maintain business interruption insurance, as well as general property insurance, the amount of insurance coverage may not be sufficient to cover our losses in such an event. Any of these occurrences could impair our ability to adequately stock our stores or fulfill customer orders and harm our operating results.

Any disruption of the supply of products from our vendors could have an adverse impact on our net sales and profitability.

We cannot predict when, or the extent to which, we will experience any disruption in the supply of products from our vendors. Any such disruption could negatively impact our ability to market and sell our products and serve our customers, which could adversely impact our net sales and profitability.

We depend on merchandise purchased from our vendors to obtain products for our stores. We have no contractual arrangements providing for continued supply from our key vendors, and our vendors may discontinue selling to us at any time. Changes in commercial practices of our key vendors or manufacturers, such as changes in vendor support and incentives or changes in credit or payment terms, could also negatively impact our results. If we lose one or more key vendors or are unable to promptly replace a vendor that is unwilling or unable to satisfy our requirements with a vendor providing equally appealing products at comparable prices, we may not be able to offer products that are important to our merchandise assortment.

We also are subject to risks, such as the price and availability of raw materials and fabrics, labor disputes, union organizing activity, strikes, inclement weather, natural disasters, war and terrorism and adverse general economic and political conditions, that might limit our vendors’ ability to provide us with quality merchandise on a timely and cost-efficient basis. We may not be able to develop relationships with new vendors, and products from alternative sources, if any, may be of a lesser quality and more expensive than those we currently purchase. Any delay or failure in offering products to our customers could have a material adverse impact on our net sales and profitability.

In addition, the SEC has adopted rules regarding disclosure of the use of conflict minerals (commonly referred to as tantalum, tin, tungsten and gold), which are mined from the Democratic Republic of the Congo and surrounding countries. We have incurred costs to design and implement a process to discover the origin of the tantalum, tin, tungsten and gold used in the products we sell, and may incur costs to audit our conflict minerals disclosures. Our reputation may also suffer if the products we sell contain conflict minerals originating in the Democratic Republic of the Congo or surrounding countries.

Political and economic uncertainty and unrest in foreign countries where our merchandise vendors are located and trade restrictions upon imports from these foreign countries could adversely affect our ability to source merchandise and operating results.

In fiscal year 2015, approximately 2.2% of our merchandise was imported directly from vendors located in foreign countries, with a substantial portion of the imported merchandise being obtained directly from vendors in China and El Salvador. In addition, we believe that a significant portion of our domestic vendors obtain their products from foreign countries that may also be subject to political and economic uncertainty. We are subject to risks and uncertainties associated with changing economic, political and other conditions in foreign countries where our vendors are located, such as:

- increased import duties, tariffs, trade restrictions and quotas;

- work stoppages;
- economic uncertainties;
- adverse foreign government regulations;
- wars, fears of war and terrorist attacks and organizing activities;
- adverse fluctuations of foreign currencies;
- natural disasters; and
- political unrest.

We cannot predict when, or the extent to which, the countries in which our products are manufactured will experience any of the above events. Any event causing a disruption or delay of imports from foreign locations would likely increase the cost or reduce the supply of merchandise available to us and would adversely affect our operating results.

In addition, trade restrictions, including increased tariffs or quotas, embargoes, safeguards and customs restrictions against clothing items, as well as U.S. or foreign labor strikes, work stoppages or boycotts could increase the cost or reduce the supply of merchandise available to us or may require us to modify our current business practices, any of which could hurt our profitability.

Finally, potential changes in federal restrictions on the importation of firearms and ammunition products could affect our ability to acquire certain popular brands of firearms and ammunition products from importers and wholesalers, which could negatively impact our net sales until replacements in the United States can be obtained, if at all.

A failure in our e-commerce operations, security breaches and cyber security risks could disrupt our business and lead to reduced sales and growth prospects and reputational damage.

Our e-commerce business is an important element of our brand and relationship with our customers, and we expect it to continue to grow. In addition to changing consumer preferences and shifting traffic patterns and buying trends in e-commerce, we are vulnerable to additional risks and uncertainties associated with e-commerce sales, including rapid changes in technology, website downtime and other technical failures, security breaches, cyber-attacks, consumer privacy concerns, changes in state tax regimes and government regulation of internet activities. Our failure to successfully respond to these risks and uncertainties could reduce our e-commerce sales, increase our costs, diminish our growth prospects and damage our brand, which could negatively impact our results of operations and stock price.

In addition, there is no guarantee that we will be able to expand our e-commerce business. Many of our competitors already have e-commerce businesses that are substantially larger and more developed than ours, which places us at a competitive disadvantage. In addition, there are regulatory restrictions on the sale of approximately 30% of our product offerings, such as ammunition, certain cutlery, firearms, propane and reloading powder. If we are unable to expand our e-commerce business, our growth plans will suffer and the price of our common stock could decline.

We do not collect sales taxes in some jurisdictions, which could result in substantial tax liabilities and cause our future e-commerce sales to decrease.

An increasing number of states have considered or adopted laws that attempt to impose tax collection obligations on out-of-state retailers. We believe that these initiatives are inconsistent with the United States Supreme Court's holding that states, absent congressional legislation, may not impose tax collection obligations on out-of-state e-commerce businesses unless the out-of-state e-commerce business has nexus with the state. A successful assertion by one or more states requiring us to collect taxes where we do not do so could result in substantial tax liabilities, including for past sales, as well as penalties and interest. The imposition by state governments of sales tax collection obligations on out-of-state e-commerce businesses who participate in e-commerce could also create additional administrative burdens for us, put us at a competitive disadvantage if they do not impose similar obligations on our competitors and decrease our future e-commerce sales, which could have a material adverse impact on our business and results of operations.

Current and future government regulations, in particular regulations relating to the sale of firearms and ammunition, may negatively impact the demand for our products and our ability to conduct our business.

We operate in a complex regulatory and legal environment that could negatively impact the demand for our products and expose us to compliance and litigation risks, which could materially affect our operations and financial results. These laws may change, sometimes significantly, as a result of political, economic or social events. Some of the federal, state or local laws and regulations that affect our business and demand for our products include:

- federal, state or local laws and regulations or executive orders that prohibit or limit the sale of certain items we offer, such as firearms, black powder firearms, ammunition, bows, knives and similar products;
- the ATF, regulations, audit and regulatory policies that impact the process by which we sell firearms and ammunition and similar policies of state agencies that have concurrent jurisdiction, such as the CA DOJ;

- laws and regulations governing hunting and fishing;
- laws and regulations relating to the collecting and sharing of non-public customer information;
- laws and regulations relating to consumer products, product liability or consumer protection, including regulation by the Consumer Product Safety Commission and similar state regulatory agencies;
- laws and regulations relating to the manner in which we advertise, market or sell our products;
- labor and employment laws, including wage and hour laws;

- U.S. customs laws and regulations pertaining to proper item classification, quotas and the payment of duties and tariffs; and
- FTC regulations governing the manner in which orders may be solicited and prescribing other obligations in fulfilling orders and consummating sales.

Over the past several years, bills have been introduced in the United States Congress that would restrict or prohibit the manufacture, transfer, importation or sale of certain calibers of handgun ammunition, impose a tax and import controls on bullets designed to penetrate bullet-proof vests, impose a special occupational tax and registration requirements on manufacturers of handgun ammunition and increase the tax on handgun ammunition in certain calibers. Because we carry these products, such legislation could, depending on its scope, materially harm our sales.

Additionally, state and local governments have proposed laws and regulations that, if enacted, would place additional restrictions on the manufacture, transfer, sale, purchase, possession and use of firearms, ammunition and shooting-related products. For example, in response to the Sandy Hook Elementary shooting in Newtown, Connecticut and other incidents in the United States, several states, such as Colorado, Connecticut, Maryland, New Jersey, and New York, have enacted laws and regulations that limit access to and sale of certain firearms in ways more restrictive than federal laws. Other state or local governmental entities may continue to explore similar legislative or regulatory restrictions that could prohibit the manufacture, sale, purchase, possession or use of firearms and ammunition. In New York and Connecticut, mandatory screening of ammunition purchases is now required. In addition, California and the District of Columbia have adopted requirements for micro-stamping (that is, engraving the handgun’s serial number on the firing pin of new handguns), and at least seven other states and the United States Congress have introduced microstamping legislation for certain firearms. Lastly, some states prohibit the sale of firearms without internal or external locking mechanisms, and several states are considering mandating certain design features on safety grounds, most of which would be applicable only to handguns. Other state or local governmental entities may also explore similar legislative or regulatory initiatives that may further restrict the manufacture, sale, purchase, possession or use of firearms, ammunition and shooting-related products.

The regulation of firearms, ammunition and shooting-related products may become more restrictive in the future. Changes in these laws and regulations or additional regulation, particularly new laws or increased regulations regarding sales and ownership of firearms and ammunition, could cause the demand for and sales of our products to decrease and could materially adversely impact our net sales and profitability. Sales of firearms represent a significant percentage of our net sales and are critical in drawing customers to our stores. A substantial reduction in our sales or margins on sales of firearms and firearm related products due to the establishment of new regulations could harm our operating results. Moreover, complying with increased or changed regulations could cause our operating expenses to increase.

We may incur costs from litigation relating to products that we sell, particularly firearms and ammunition, which could adversely affect our net sales and profitability.

We may incur damages due to lawsuits relating to products we sell, including lawsuits relating to firearms, ammunition, tree stands and archery equipment. We may incur losses due to lawsuits, including potential class actions, relating to our performance of background checks on firearms purchases and compliance with other sales laws as mandated by state and federal law. We may also incur losses from lawsuits relating to the improper use of firearms or ammunition sold by us, including lawsuits by municipalities or other organizations attempting to recover costs from manufacturers and retailers of firearms and ammunition. Our insurance coverage and the insurance provided by our vendors for certain products they sell to us may be inadequate to cover claims and liabilities related to products that we sell. In addition, claims or lawsuits related to products that we sell, or the unavailability of insurance for product liability claims, could result in the elimination of these products from our product line, thereby reducing net sales. If one or more successful claims against us are not covered by or exceed our insurance coverage, or if insurance coverage is no longer available, our available working capital may be impaired and our operating results could be materially adversely affected. Even unsuccessful claims could result in the expenditure of funds and management time and could have a negative impact on our profitability and on future premiums we would be required to pay on our insurance policies.

If we fail to maintain the strength and value of our brand, our net sales are likely to decline.

Our success depends on the value and strength of the Sportsman's Warehouse brand. The Sportsman's Warehouse name is integral to our business as well as to the implementation of our strategies for expanding our business. Maintaining, promoting and positioning our brand will depend largely on the success of our marketing and merchandising efforts and our ability to provide high quality merchandise and a consistent, high quality customer experience. Our brand could be adversely affected if we fail to achieve these objectives or if our public image or reputation were to be tarnished by negative publicity. Any of these events could result in decreases in net sales.

Our inability or failure to protect our intellectual property could have a negative impact on our operating results.

Our trademarks, service marks, copyrights, patents, trade secrets, domain names and other intellectual property are valuable assets that are critical to our success. The unauthorized reproduction or other misappropriation of our intellectual property could diminish the value of our brands or goodwill and cause a decline in our net sales. Any infringement or other intellectual property claim made against us, whether or not it has merit, could be time-consuming, result in costly litigation, cause product delays or require us to enter into royalty or licensing agreements. As a result, any such claim could have a material adverse effect on our operating results.

Unauthorized disclosure of sensitive or confidential customer information could harm our business and standing with our customers.

The protection of our customer, employee and company data is critical to us. We rely on commercially available systems, software, tools and monitoring to provide security for processing, transmission and storage of confidential customer information, such as payment card and personally identifiable information. Despite the security measures we have in place, our facilities and systems, and those of our third-party service providers, may be vulnerable to security breaches, acts of vandalism, computer viruses, misplaced or lost data, programming or human errors or other similar events. Any security breach involving the misappropriation, loss or other unauthorized disclosure of confidential information, whether by us or our vendors, could damage our reputation, expose us to risk of litigation and liability, disrupt our operations and harm our business.

Our computer hardware and software systems are vulnerable to damage that could harm our business.

Our success, in particular our ability to successfully manage inventory levels, largely depends upon the efficient operation of our computer hardware and software systems. We use management information systems to track inventory information at the store level, communicate customer information and aggregate daily sales, margin and promotional information. These systems are vulnerable to damage or interruption from:

- fire, flood, tornado and other natural disasters;
- power loss, computer system failures, internet and telecommunications or data network failures, operator negligence, improper operation by or supervision of employees, physical and electronic loss of data or security breaches, misappropriation and similar events;
- hacking by third parties and computer viruses; and
- upgrades, installations of major software releases and integration with new systems.

Any failure that causes an interruption in our systems processing could disrupt our operations and result in reduced sales. We have centralized the majority of our computer systems in our corporate office. It is possible that an event or disaster at our corporate office could materially and adversely affect the performance of our company and the ability of each of our stores to operate efficiently.

Our private brand offerings expose us to various risks.

We expect to continue to grow our exclusive private brand offerings through a combination of brands that we own and brands that we license from third parties. We have invested in our development and procurement resources and marketing efforts relating to these private brand offerings. Although we believe that our private brand products offer value to our customers at each price point and provide us with higher gross margins than comparable third-party branded products we sell, the expansion of our private brand offerings also subjects us to certain specific risks in addition to those discussed elsewhere in this section, such as:

- potential mandatory or voluntary product recalls;
- our ability to successfully protect our proprietary rights (including defending against counterfeit, knock offs, grey-market, infringing or otherwise unauthorized goods);

- our ability to successfully navigate and avoid claims related to the proprietary rights of third parties;
- our ability to successfully administer and comply with obligations under license agreements that we have with the licensors of brands, including, in some instances, certain minimum sales requirements that, if not met, could cause us to lose the licensing rights or pay damages; and
- other risks generally encountered by entities that source, sell and market exclusive branded offerings for retail.

An increase in sales of our private brands may also adversely affect sales of our vendors' products, which may, in turn, adversely affect our relationship with our vendors. Our failure to adequately address some or all of these risks could have a material adverse effect on our business, results of operations and financial condition.

If we lose key management or are unable to attract and retain the talent required for our business, our operating results and financial condition could suffer.

Our performance depends largely on the leadership efforts and abilities of our executive officers and other key employees. We have entered into employment agreements with John V. Schaefer, our President and Chief Executive Officer, and Kevan P. Talbot, our Chief Financial Officer and Secretary. None of our other employees have an employment agreement with us. If we lose the services of one or more of our key employees, we may not be able to successfully manage our business or achieve our growth objectives. As our business grows, we will need to attract and retain additional qualified personnel in a timely manner.

Our business depends on our ability to meet our labor needs.

Our success depends in part upon our ability to attract, motivate and retain a sufficient number of qualified employees, including district managers, store managers, department managers and sales associates, who understand and appreciate our outdoor culture and are able to adequately represent this culture to our customers. Qualified individuals of the requisite caliber and number needed to fill these positions may be in short supply in some areas, and the turnover rate in the retail industry is high. If we are unable to hire and retain sales associates capable of consistently providing a high level of customer service, as demonstrated by their enthusiasm for our culture and knowledge of our merchandise, our business could be materially adversely affected. Although none of our employees is currently covered by collective bargaining agreements, our employees may elect to be represented by labor unions in the future, which could increase our labor costs. Additionally, competition for qualified employees could require us to pay higher wages to attract a sufficient number of employees. An inability to recruit and retain a sufficient number of qualified individuals in the future may delay the planned openings of new stores. Any such delays, any material increases in employee turnover rates at existing stores or any increases in labor costs could have a material adverse effect on our business, financial condition or operating results.

Increases in the minimum wage could adversely affect our financial results.

From time to time, legislative proposals are made to increase the federal minimum wage in the United States, as well as the minimum wage in a number of individual states. Base wage rates for some of our employees are at or slightly above the minimum wage. As federal or state minimum wage rates increase, we may need to increase not only the wage rates of our minimum wage employees, but also the wages paid to our other hourly employees as well. Any increase in the cost of our labor could have an adverse effect on our operating costs, financial condition and results of operations.

We may pursue strategic acquisitions or investments, and the failure of an acquisition or investment to produce the anticipated results or the inability to fully integrate the acquired companies could have an adverse impact on our business.

We may from time to time acquire or invest in complementary companies, businesses or assets. The success of such acquisitions or investments will be based on our ability to make accurate assumptions regarding the valuation, operations, growth potential, integration and other factors relating to the respective business or assets. Our acquisitions or investments may not produce the results that we expect at the time we enter into or complete the transaction. For example, we may not be able to capitalize on previously anticipated synergies. Furthermore, acquisitions may result in dilutive issuances of our equity securities, the incurrence of debt, contingent liabilities, amortization expenses or write-offs of goodwill or other intangibles, any of which could harm our financial condition or results of operations. We also may not be able to successfully integrate operations that we acquire, including their personnel, financial systems, supply chain and other operations, which could adversely affect our business. Acquisitions may also result in the diversion of our capital and our management’s attention from other business issues and opportunities.

A new standard for lease accounting may significantly impact the timing and amount in which we report our lease expense.

In February 2016, the Financial Accounting Standards Board, or FASB, and the International Accounting Standards Board, or IASB, issued an accounting pronouncement with substantial changes to existing lease accounting that affects all lease arrangements. The new standard is effective beginning in the first quarter of 2019 and early adoption is permitted. Under the new accounting model, lessees are required to record an asset representing the right-to-use the leased item for the lease term, or right-of-use asset, and a corresponding liability to make lease payments. The right-of-use asset and liability incorporate the rights arising under the lease and are based on the lessee's assessment of expected payments to be made over the lease term. The model requires measuring these amounts at the present value of the future expected payments.

Once we adopt this new standard, we expect that, for the majority of our leases, the lease expense would include the amortization of the right-of-use asset and the recognition of interest expense based upon the lessee's incremental borrowing rate (or the rate implicit in the lease, if known) on the repayment of the lease obligation. Currently, management is assessing the impact the adoption of the new final lease standard will have on our financial statements. Although we believe the presentation of our financial statements will likely change, including the pattern of lease expense recognition, we do not believe the accounting pronouncement will change the fundamental economic reasons for which we lease our stores.

We may not achieve projected goals and objectives in the time periods that we anticipate or announce publicly, which could harm our business and cause the price of our common stock to decline.

We set targets and timing to accomplish certain objectives regarding our business. We have included some of these targets in this filing and may make similar future public statements. For example, we state in this filing that:

- we currently plan to open nine additional new stores in fiscal year 2016 and, for the next several years thereafter, intend to grow our store base at a rate greater than 10 percent annually; and
- we target a minimum 10% four-wall Adjusted EBITDA margin and a minimum return on invested capital of 50% excluding initial inventory cost (or 20% including initial inventory cost) in the first twelve months of operation for a new store.

This filing also includes other forecasts and targets. These forecasts and targets are based on our current expectations. We may not achieve these forecasts and targets, and the actual achievement and timing of these events can vary due to a number of factors, including currently unforeseen matters and matters beyond our control. You should not unduly rely on these forecasts or targets in deciding whether to invest in our common stock.

Risks Related to Our Common Stock

Affiliates of Seidler Equity Partners III, L.P. (collectively, “Seidler”) beneficially own approximately 36.4% of our common stock, and their interests may conflict with or differ from the interests of our other stockholders.

Seidler beneficially owns approximately 36.4% of our common stock. As a result, Seidler has significant influence over the election of all of our directors and the approval of significant corporate transactions that require the approval of our board of directors or stockholders, such as mergers and the sale of substantially all of our assets. So long as Seidler continues to own a significant amount of the outstanding shares of our common stock, it will have the ability to exert significant influence over our corporate decisions. Seidler may act in a manner that advances its best interests and not necessarily those of other stockholders by, among other things:

- delaying, deferring or preventing a change in control transaction;
- entrenching our management and/or our board of directors;
- impeding a merger, consolidation, takeover or other business combination involving us;
- discouraging a potential acquirer from making a tender offer or otherwise attempting to obtain control of us; or
- causing us to enter into transactions or agreements that are not in the best interests of all stockholders.

Additionally, Seidler is in the business of making investments in companies and may in the future acquire interests in businesses that directly or indirectly compete with certain portions of our business or our suppliers or customers. Seidler may also pursue acquisitions that may be complementary to our business, and, as a result, those acquisition opportunities may not be available to us.

Seidler and the members of our board of directors who are affiliated with Seidler, by the terms of our certificate of incorporation, are not required to offer us any transaction opportunity of which they become aware and could take any such opportunity for themselves or offer it to other companies in which they have an investment, unless such opportunity is expressly offered to them solely in their capacity as our directors. We, by the terms of our certificate of incorporation, expressly renounce any interest in any such corporate opportunity to the extent permitted under applicable law, even if the opportunity is one that we would reasonably be deemed to have pursued if given the opportunity to do so, unless such opportunity is expressly offered to any director or officer in his or her capacity as our director or officer. Our certificate of incorporation cannot be amended to eliminate our renunciation of any such corporate opportunity arising prior to the date of any such amendment. Seidler or its affiliates may also acquire competing businesses that may not be attractive to us, and have no obligation to refrain from acquiring competing businesses. Any competition could intensify if an affiliate or subsidiary of Seidler were to enter into or acquire a business similar to our specialty retail operations. Seidler or its affiliates may enter into or acquire a competing business in the future.

Although we are no longer a "controlled company" within the meaning of The NASDAQ Stock Market corporate governance standards, we may continue to rely on exemptions from some of the corporate governance requirements that provide protection to stockholders of other companies.

Affiliates of Seidler no longer control a majority of our outstanding common stock. As a result, we are no longer a "controlled company" within the meaning of The NASDAQ Stock Market corporate governance standards. The NASDAQ Stock Market corporate governance requirements require that:

- a majority of the board of directors consist of "independent directors" as defined under The NASDAQ Stock Market corporate governance standards;
- our director nominees be selected, or recommended for our board of directors' selection, either (1) by a majority of independent directors in a vote by independent directors, pursuant to a nominations process adopted by a board resolution, or (2) by a nominating and governance committee comprised solely of independent directors with a written charter addressing the nominations process; and
- the compensation of our executive officers be determined, or recommended to the board for determination, by a majority of independent directors in a vote by independent directors, or by a compensation committee comprised solely of independent directors.

Currently, a majority of our board of directors consists of independent directors, and we have an audit committee and a compensation committee comprised solely of independent directors. However, our nominating and governance committee is not comprised solely of independent directors. The rules of The NASDAQ Stock Market require that our nominating and governance committee be composed entirely of independent directors within one year of closing our secondary public offering in September 2015, or by September 30, 2016. During this transition period, however, we could avail ourselves of any of the exemptions described above even if we are not currently relying upon them. Accordingly, during this transition period, our stockholders may not have the same protections afforded to stockholders of companies that are subject to all of The NASDAQ Stock Market corporate governance standards.

Our bylaws, our certificate of incorporation and Delaware law contain provisions that could discourage another company from acquiring us and may prevent attempts by our stockholders to replace or remove our current management.

Provisions of our bylaws, our certificate of incorporation and Delaware law may discourage, delay or prevent a merger or acquisition that stockholders may consider favorable, including transactions in which our stockholders might otherwise receive a premium for their shares. In addition, these provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace or remove our board of directors. These provisions include:

- establishing a classified board of directors;
- providing that directors may be removed only for cause;
- not providing for cumulative voting in the election of directors;
- requiring at least a supermajority vote of our stockholders to amend our bylaws or certain provisions of our certificate of incorporation;
- eliminating the ability of stockholders to call special meetings of stockholders;
- establishing advance notice requirements for nominations for election to the board of directors or for proposing matters that can be acted on by stockholders at stockholder meetings;
- prohibiting stockholder action by written consent once Seidler owns less than a majority of the outstanding shares of our common stock; and
- authorizing the issuance of "blank check" preferred stock without any need for action by stockholders.

In addition, we will be subject to Section 203 of the Delaware General Corporation Law once Seidler ceases to beneficially own at least 15% of the total voting power of our then-outstanding shares of common stock. In general, subject to some exceptions, Section 203 prohibits a Delaware corporation from engaging in any "business combination" with any "interested stockholder" (which is generally defined as an entity or person who, together with the person's affiliates and associates, beneficially owns, or within three years prior to the time of determination of interested stockholder status did own, 15% or more of the outstanding voting stock of the corporation), for a three-year period following the date that the stockholder became an interested stockholder. Section 203 could have the effect of delaying, deferring or preventing a change in control that our stockholders might consider to be in their best interests.

Further, our certificate of incorporation provides that, subject to limited exceptions, the Court of Chancery of the State of Delaware will be, to the fullest extent permitted by law, the exclusive forum for any derivative action or proceeding brought on our behalf; any action asserting a breach of fiduciary duty; any action asserting a claim against us arising pursuant to the Delaware General Corporation Law; or any action asserting a claim against us that is governed by the internal affairs doctrine. This exclusive forum provision may limit a stockholder’s ability to bring a claim in a judicial forum that it finds favorable for disputes with us or our directors, officers or other employees and agents, which may discourage such lawsuits against us and our directors, officers, employees and agents.

Together, these charter and statutory provisions could make the removal of management more difficult and may discourage transactions that otherwise could involve payment of a premium over prevailing market prices for our common stock. The existence of the foregoing provisions and anti-takeover measures could limit the price that investors might be willing to pay in the future for shares of our common stock. They could also deter potential acquirers of our company, thereby potentially reducing the likelihood that our stockholders could receive a premium for their common stock in an acquisition.

We expect that the price of our common stock will fluctuate.

Volatility in the market price of our common stock may prevent our stockholders from being able to sell their common stock at or above the prices they paid for their common stock. The market price for our common stock could fluctuate significantly for various reasons, including:

- our operating and financial performance and prospects, including seasonal fluctuations in our financial performance;
- conditions that impact demand for our products;
- the public’s reaction to our press releases, other public announcements and filings with the SEC;
- changes in earnings estimates or recommendations by securities analysts who track our common stock;
- market and industry perception of our success, or lack thereof, in pursuing our growth strategy;
- strategic actions by us or our competitors, such as acquisitions or restructurings;
- changes in federal and state government regulation;
- changes in accounting standards, policies, guidance, interpretations or principles;
- arrival or departure of key personnel;
- sales of common stock by us or members of our management team; and
- changes in general market, economic and political conditions in the United States and global economies or financial markets, including those resulting from natural disasters, terrorist attacks, acts of war and responses to such events.

In addition, if the market for stocks in our industry, or the stock market in general, experiences a loss of investor confidence, the trading price of our common stock could decline for reasons unrelated to our business, financial condition or results of operations. If any of the foregoing occurs, it could cause our stock price to fall and may expose us to lawsuits that, even if unsuccessful, could be costly to defend and distract our management.

We are an emerging growth company (“EGC”) within the meaning of The Jumpstart our Business Startups Act (“JOBS Act”), and the reduced reporting requirements applicable to EGCs may make our common stock less attractive to investors.

Because we qualify as an EGC under the JOBS Act, we have elected to comply with some of the reduced disclosure and other reporting requirements available to us as an EGC for a period of up to five years following our initial public offering if we remain an EGC. For example, for as long as we remain an EGC, we are not subject to certain governance requirements, such as holding a “say-on-pay” and “say-on-golden-parachute” advisory votes, we are not required to include a “Compensation Discussion and Analysis” section in our proxy statements and reports filed under the Exchange Act, and we do not need to obtain an annual attestation report on our internal control over financial reporting from a registered public accounting firm pursuant to Section 404(b) of the Sarbanes-Oxley Act of 2002 (the “Sarbanes-Oxley Act”). We could be an EGC for a period up to the end of the fifth fiscal year after our initial public offering, although we will cease to be an EGC earlier than this five-year period if our total annual gross revenues equal or exceed $1 billion in a fiscal year, if we issue more than $1 billion in non-convertible debt over a three-year period or if we become a “large accelerated filer” (which requires, among other things, the market value of our common stock held by non-affiliates to be at least $700 million as of the last business day of our second fiscal quarter of any fiscal year).

Accordingly, for up to five fiscal years after our initial public offering, our stockholders may not receive the same level of disclosure that is afforded to stockholders of a non-EGC. It is possible that investors will find our common stock to be less attractive because we have elected to comply with the reduced disclosure and other reporting requirements available to us as an EGC, which could adversely affect the trading market for our common stock and the prices at which stockholders may be able to sell their common stock.

The requirements of being a public company may strain our resources and divert management's attention.

As a public company, we are subject to the reporting requirements of the Exchange Act, the Sarbanes-Oxley Act, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 and other applicable securities rules and regulations. Compliance with these rules and regulations have increased our legal and financial compliance costs, make some activities more difficult, time-consuming or costly and increase demand on our systems and resources. The Exchange Act requires, among other things, that we file annual, quarterly and current reports with respect to our business and results of operations and proxy or information statements in connection with matters upon which our stockholders may vote. As a result of our public disclosure of information in filings required of a public company, our business and financial condition have become more visible, which could result in threatened or actual litigation, or other adverse actions taken by competitors and other third parties. In addition, our management team has limited experience managing a public company or complying with the increasingly complex laws pertaining to public companies, and a number of our directors have limited experience serving on the boards of public companies. The time and resources necessary to comply with the requirements of being a public company and contend with any action that might be brought against us as a result of publicly available information could divert our resources and the attention of our management and adversely affect our business, financial condition and results of operations.

If we are unable to implement and maintain effective internal control over financial reporting, investors may lose confidence in the accuracy and completeness of our financial reports, and the market price of our common stock may be adversely affected.

As a public company, we are required to implement and maintain effective internal control over financial reporting and to disclose any material weaknesses identified in our internal controls. Our management is required to furnish an annual report regarding the effectiveness of our internal control over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act ("Section 404"). We have refined, implemented, and tested the internal controls required to comply with Section 404. If we identify material weaknesses in our internal control over financial reporting, if we fail to comply with the requirements of Section 404 in a timely manner or if we are unable to assert that our internal control over financial reporting is effective, investors may lose confidence in the accuracy and completeness of our financial reports and the market price of our common stock could be adversely affected. We could also become subject to investigations by The NASDAQ Stock Market, the SEC or other regulatory authorities, which could require additional financial and management resources.

We do not expect to pay any cash dividends for the foreseeable future.

We currently expect to retain all available funds and future earnings, if any, for use in the operation and growth of our business and do not anticipate paying any cash dividends in the foreseeable future. Any future determination to pay dividends will be at the discretion of our board of directors, subject to compliance with applicable law and any contractual provisions, including under the credit agreements governing our term loans and revolving credit facility and agreements governing any additional indebtedness we may incur in the future, that restrict or limit our ability to pay dividends, and will depend upon, among other factors, our results of operations, financial condition, earnings, capital requirements and other factors that our board of directors deems relevant. Further, because we are a holding company, our ability to pay dividends depends on our receipt of cash dividends from our operating subsidiaries, which may further restrict our ability to pay dividends as a result of the laws of their jurisdiction of organization, agreements of our subsidiaries or covenants under our existing or future indebtedness. All of our business operations are conducted through our wholly owned subsidiaries, Sportsman's Warehouse, Inc. and Minnesota Merchandising

Corporation and their subsidiaries. The ability of Sportsman's Warehouse, Inc. and Minnesota Merchandising Corporation to pay dividends to us, and our ability to pay dividends on our capital stock, is limited by our term loans. Our revolving credit facility also limits our ability to pay dividends on our capital stock. Our ability to pay dividends may also be restricted by the terms of any future credit agreement or any future debt or preferred equity securities of ours or of our subsidiaries.

If securities or industry analysts publish inaccurate or unfavorable research about us, our stock price and trading volume could decline.

The trading market for our common stock will depend in part on the research reports that securities or industry analysts publish about us, our business and our industry. Assuming we obtain securities or industry analyst coverage, if one or more of the analysts who cover us downgrade our stock or publish inaccurate or unfavorable research about us, our business or our industry, our stock price would likely decline. If one or more of these analysts cease coverage of our company or fail to publish reports on us regularly, demand for our stock could decrease, which might cause our stock price and trading volume to decline.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We do not plan to own any material real property, but rather intend to lease all of our store locations. From time to time we will self-develop one of our properties with the intention to enter into a sale-leaseback transaction with a third party. Depending upon where we are in the process of completing the sale-leaseback transaction, we may legally own real property at any particular balance sheet date. Our corporate headquarters is located in an approximately 60,000 square foot building in Midvale, Utah. The building is leased under an agreement expiring on December 31, 2018.

Our distribution center is located in a 507,000 square foot facility in Salt Lake City, Utah. The building is leased under an agreement expiring on December 31, 2023, with three options that each allow us to extend for an additional five years. We believe that our distribution center is of sufficient scale to support a network of up to 100 stores.

We operate 66 retail stores in 20 states. In total we have approximately 2.8 million gross square feet across all of our stores. All of our stores are leased from third parties with lease terms typically ranging from five to fifteen years, and many of our lease agreements have additional five-year renewal options. All of our leases provide for additional payments associated with common area maintenance, real estate, taxes and insurance. In addition, many of our lease agreements have defined escalating rent provisions over the initial term and extensions.

ITEM 3. LEGAL PROCEEDINGS

On March 11, 2013, we acquired certain assets and assumed certain liabilities of Wholesale Sports Outdoor Outfitters, or Wholesale Sports, relating to their retail business of hunting, fishing and camping goods and supplies. Concurrently with our asset purchase, Alamo Group, LLC, an unrelated third party, purchased all of the stock of Wholesale Sports. On March 22, 2013, the landlord of a store in Spokane, Washington that was formerly operated by Wholesale Sports, and which was one of the five stores whose leases we did not assume in our purchase of assets from Wholesale Sports, filed a complaint against the seller of Wholesale Sports, Wholesale Sports and Alamo Group in the Superior Court for the State of Washington in the County of Spokane captioned as North Town Mall v. United Farmers of Alberta Co-Operative Limited, et al., Case No. 13-2-01201-9. The complaint, as amended, alleged claims for breach of lease, violation of Washington’s Fraudulent Transfer Act, tortious interference with contractual relations, piercing the corporate veil, assumption of the Spokane store lease and fraud and/or negligent representation. We were named as a co-defendant in the amended complaint with respect to the fraudulent conveyance, tortious interference, and assumption of the lease claims. The complaint requested that the court order “avoidance” of an alleged transfer of assets from Wholesale Sports to us and/or Alamo Group, damages based on future rent to be paid under the lease in the approximate amount of $4.5 million, attachment of assets, attorneys’ fees and costs as provided for in contract, and such other relief that the court deems just and proper. In addition, the amended complaint alleged that we and Alamo Group were liable for expenses that the landlord would incur as a result of default under the lease, including expenses related to returning the store premises to the condition called for in the lease and the cost to locate a new tenant.

On March 12, 2014, we were added as a defendant to a pending consolidated action filed in the United States District Court, Western District of Washington, captioned as Lacey Market Place Associates II, LLC, et al. v. United Farmers of Alberta Co-Operative Limited, et al., Case No. 2:13-cv-00383-JLR against United Farmers of Alberta Co-Operative Limited, the seller of Wholesale Sports, Wholesale Sports, Alamo Group and Donald F. Gaube and spouse. The amended complaint was filed by the landlords of two stores we did not assume in our purchase of assets from Wholesale Sports. Such stores were formerly operated by Wholesale Sports in Skagit and Thurston Counties in Washington. The amended complaint alleged breach of lease, breach of collateral assignment, misrepresentation, intentional interference with contract, piercing the corporate veil and violation of Washington’s Fraudulent Transfer Act. We were named as a co-defendant with respect to the intentional interference with contract and fraudulent conveyance claims. The amended complaint sought against us and all defendants unspecified money damages, declaratory relief and attorneys' fees and costs. On January 28, 2015, the court in the Lacey Marketplace action granted in part and denied in part our motion for summary judgment and dismissed the intentional interference claim against us, but declined to dismiss the fraudulent transfer claim.

Trial in the Lacey Marketplace action began March 2, 2015 and concluded March 6, 2015. On March 9, 2015, the jury in the trial awarded $11.9 million against the defendants to the action, including us. We reviewed the decision and accrued $4.0 million in our results for the fiscal year ended January 31, 2015 related to this matter. We strongly disagreed with the jury’s verdict and filed post-trial motions seeking to have the verdict set aside. On July 30, 2015, the court granted our motion for judgment as a matter of law. Both United Farmers of Alberta Co-Operative Limited, a co-defendant, and the plaintiff have appealed the court’s summary judgment ruling against the tortious interference claim, and the July 30, 2015 ruling to the appellate court and the appeal is currently in process. Based on the court’s most recent judgment in our favor, we determined that the likelihood of loss in this case is not probable, and, as such, we reversed the previous accrual of $4.0 million in our results for the fiscal year ended January 30, 2016. The accrual and subsequent reversal of the $4.0 million is recorded in selling, general, and administrative expenses in the accompanying statements of income.

When we become aware of a claim or potential claim, we assess the likelihood of any loss or exposure. If a loss contingency is probable and the amount of the loss can be reasonably estimated, we record an accrual for the loss. In such cases, there may be an exposure to potential loss in excess of the amount accrued. Where a loss is not probable but is reasonably possible or where a loss in excess of the amount accrued is reasonably possible, we disclose an estimate of the amount of the loss or range of possible losses for the claim if a reasonable estimate can be made, unless the amount of such reasonably possible losses is not material to our financial position, results of operations or cash flows. The ability to predict the ultimate outcome of such matter involves judgments and inherent uncertainties. The actual outcome could differ.

We are subject to various legal proceedings and claims, including employment claims, wage and hour claims, intellectual property claims, contractual and commercial disputes and other matters that arise in the ordinary course of our business. While the outcome of these and other claims cannot be predicted with certainty, we do not believe that the outcome of these matters individually or in the aggregate will have a material adverse effect on our business, results of operations or financial condition.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED STOCKHODLER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market for Registrant’s Common Equity

The common stock of Sportsman’s Warehouse Holdings Incorporated is listed for trading on the NASDAQ under the symbol “SPWH." As of February 29, 2016, there were 92 holders of record of our common stock. This number does not include persons who hold our common stock in nominee or “street name” accounts through brokers or banks.

The following table sets forth, for the fiscal quarters indicated, the high and low sales prices per share of our common stock as reported on the NASDAQ:

	2015	
	High	Low
First Quarter	9.73	6.81
Second Quarter	12.88	9.18
Third Quarter	14.91	9.92
Fourth Quarter	13.78	9.26

	2014	
	High	Low
First Quarter	10.90	9.47
Second Quarter	10.10	5.79
Third Quarter	7.67	5.46
Fourth Quarter	8.10	6.29

Dividend Policy

We did not pay any dividends in fiscal year 2015 or fiscal year 2014.

We currently expect to retain all available funds and future earnings, if any, for use in the operation and growth of our business and do not anticipate paying any cash dividends in the foreseeable future. Any future determination to pay dividends will be at the discretion of our board of directors, subject to compliance with applicable law and any contractual provisions, including under the credit agreements governing our term loans and revolving credit facility and agreements governing any additional indebtedness we may incur in the future, that restrict or limit our ability to pay dividends, and will depend upon, among other factors, our results of operations, financial condition, earnings, capital requirements and other factors that our board of directors deems relevant. Because we are a holding company, our ability to pay dividends depends on our receipt of cash dividends from our operating subsidiaries, which may further restrict our ability to pay dividends as a result of the laws of their jurisdiction of organization, agreements of our subsidiaries or covenants under our existing or future indebtedness. All of our business operations are conducted through our wholly owned subsidiaries, Sportsman’s Warehouse, Inc. and Minnesota Merchandising Corporation and their subsidiaries. The ability of Sportsman’s Warehouse, Inc. and Minnesota Merchandising Corporation to pay dividends to us, and our ability to pay dividends on our capital stock, is limited by our term loans. Our revolving credit facility also limits our ability to pay dividends on our capital stock. Our ability to pay dividends may also be restricted by the terms of any future credit agreement or any future debt or preferred equity securities of ours or of our subsidiaries.

Equity Compensation Plan Information

Equity compensation plan information required by this Item 5 will be included in our definitive proxy statement for our annual meeting of stockholders, which will be filed with the SEC no later than 120 days after the end of our fiscal year ended January 30, 2016 (the "Proxy Statement"), and is incorporated herein by reference.

Stock Performance Graph

The stock price performance graph below shall not be deemed soliciting material or to be filed with the SEC or subject to Regulation 14A or 14C under the Exchange Act or to the liabilities of Section 18 of the Exchange Act, nor shall it be incorporated by reference into any past or future filing under the Securities Act of 1933, as amended, or the Securities Act or the Exchange Act, except to the extent we specifically request that it be treated as soliciting material or specifically incorporate it by reference into a filing under the Securities Act or the Exchange Act.

The following graph shows the cumulative total stockholder return of an investment of $100 in cash at market close on April 17, 2014 (the first day of trading of our Common Stock), through January 29, 2016 for (i) our Common Stock (“SPWH”), (ii) the S&P 500 Retailing Industry Group Index (“S&P Retail”) and (iii) the Russell 2000 Index (“Russell 2000”). Pursuant to applicable SEC rules, all values assume reinvestment of the full amount of all dividends. The stockholder return shown on the graph below is not necessarily indicative of future performance, and we do not make or endorse any predictions as to future stockholder returns.

	4/17/2014	5/2/2014	8/1/2014	10/31/2014	1/30/2015	5/1/2015	7/31/2015	10/30/2015	1/29/2016
SPWH	$ 100.00	$ 103.38	$ 59.38	$ 71.69	$ 73.13	$ 96.51	$ 119.90	$ 110.36	$ 134.46
S&P Retail	100.00	99.81	101.23	109.99	118.76	130.94	141.46	148.43	137.24
Russell 2000	100.00	99.20	97.98	103.13	102.42	107.93	108.86	102.11	90.99

ITEM 6. SELECTED FINANCIAL DATA.

	Fiscal Year Ended		
	January 30, 2016	January 31, 2015	February 1, 2014
	(in thousands, except per share amounts)		
Consolidated Statements of Income Data:			
Net sales	$729,912	$660,003	$ 643,163
Cost of goods sold	491,382	444,796	435,933
Gross profit	238,530	215,207	207,230
Selling, general and administrative expenses	179,218	170,315	147,140
Bankruptcy-related expenses (1)	—	—	55
Income from operations	59,312	44,892	60,035
Interest expense	(14,156)	(22,480)	(25,447)
Income before income taxes	45,156	22,412	34,588
Income tax expense	17,385	8,628	12,838
Net income	$27,771	$13,784	$ 21,750
Earnings per share:			
Basic	$0.66	$0.34	$ 0.66
Diluted	$0.66	$0.34	$ 0.66
Weighted average shares outstanding:			
Basic shares	41,966	39,961	33,170
Diluted shares	42,334	40,141	33,185

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	Fiscal Year Ended January 30, 2016	January 31, 2015	February 1, 2014
	(in thousands, except number of stores and per share amounts)		
Consolidated Balance Sheet Data:			
Total current assets	$233,059	$203,671	$176,316
Total assets	303,024	270,723	224,229
Long-term debt (including current portion), net of discount	156,712	158,046	231,132
Total liabilities	305,083	302,055	345,325
Total stockholders' deficit	(2,059)	(31,332)	(121,096)
Total liabilities and stockholders' deficit	303,024	270,723	224,229
Other Data:			
Adjusted EBITDA (2)	$73,024	$66,252	$70,716
Adjusted EBITDA margin (2)	10.0%	10.0%	10.9%
Number of stores open at end of period	64	55	47
Same store sales growth for period (3)	1.1%	(8.4)%	(3.7)%
Cash dividend declared per common share (on a pre-split basis)	$—	$—	$8.73

(1) On March 21, 2009, Sportsman's Warehouse Holdings, Inc. and its subsidiaries filed voluntary petitions for relief under Chapter 11 of the United States Bankruptcy Code, seeking to reorganize the business under the provisions of the Bankruptcy Code. The plan of reorganization under the Bankruptcy Code was confirmed by the United States Bankruptcy Court for the District of Delaware on July 30, 2009 and became effective when all material conditions of the plan of reorganization were satisfied on August 14, 2009. We incurred certain costs related to our restructuring and emergence from Chapter 11 bankruptcy and included a liability as part of the reorganization value at August 14, 2009, the date of emergence from bankruptcy. Bankruptcy-related expenses are those amounts that are greater than the initial estimated restructuring costs. They are expensed as incurred.

(2) Adjusted EBITDA has been presented in this filing as a supplemental measure of financial performance that is not required by, or presented in accordance with, generally accepted accounting principles, or GAAP. We define Adjusted EBITDA as net income plus interest expense, income tax expense, depreciation and amortization, stock-based compensation expense, pre-opening expenses, and other gains, losses, and expenses that we do not believe are indicative of our ongoing expenses. Adjusted EBITDA margin means, for any period, the Adjusted EBITDA for that period divided by the net sales for that period.

Adjusted EBITDA and Adjusted EBITDA margin are included in this filing because they are key metrics used by management and our board of directors to assess our financial performance. Adjusted EBITDA and Adjusted EBITDA margin are frequently used by analysts, investors and other interested parties in the evaluation of companies in our industry. In addition to assessing our financial performance, we use Adjusted EBITDA and Adjusted EBITDA margin as additional measurement tools for purposes of business decision-making, including evaluating store performance, developing budgets and managing expenditures.

Adjusted EBITDA is not a GAAP measure of our financial performance or liquidity and should not be considered as an alternative to net income as a measure of financial performance or cash flows from operations as a measure of liquidity, or any other performance measure derived in accordance with GAAP, and it should not be construed as an inference that our future results will be unaffected by unusual or non-recurring items. Additionally, Adjusted EBITDA is not intended to be a measure of free cash flow for management's discretionary use, as it does not reflect certain cash requirements such as tax payments, debt service requirements, capital expenditures, store openings and certain other cash costs that may recur in the future. Adjusted EBITDA contains certain other limitations, including the failure to reflect our cash expenditures or future requirements for capital expenditures or contractual commitments. In evaluating Adjusted EBITDA, you should be aware that, in the future, we will incur expenses that are the same as or similar to some of the adjustments reflected in this presentation, such as income tax expense (benefit), interest expense, depreciation and amortization and pre-opening expenses. Our presentation of Adjusted EBITDA should not be construed to imply that our future results will be unaffected by any such adjustments. Management compensates for these limitations by relying on our GAAP results in addition to using Adjusted EBITDA supplementally. Our measures of Adjusted EBITDA are not necessarily comparable to other similarly titled captions of other companies due to different methods of calculation. See below for a reconciliation of net income to Adjusted EBITDA.

(3) Net sales from a store are included in same store sales on the first day of the 13th full month following the store's opening or acquisition by us. We exclude net sales from e-commerce from our calculation of same store sales, and for fiscal years consisting of 53 weeks, we exclude net sales during the 53rd week from our calculation of same store sales. The figures shown represent growth over the corresponding period in the prior fiscal year.

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A reconciliation of net income to Adjusted EBITDA is set forth below:

	Fiscal Year Ended January 30, 2016	January 31, 2015	February 1, 2014
	(in thousands)		
Net income	$27,771	$13,784	$ 21,750
Plus:			
Interest expense	14,156	22,480	25,447
Income tax expense	17,385	8,628	12,838
Depreciation and amortization	11,569	9,150	6,277
Stock-based compensation expense (a)	2,257	3,293	365
Pre-opening expenses (b)	3,159	2,717	1,653
IPO bonus (c)	—	2,200	—
Litigation accrual (reversal) (d)	(4,000)	4,000	—
Bankruptcy-related expenses (e)	—	—	55
Acquisition expenses (f)	—	—	2,331
Secondary offering expenses (g)	727	—	—
Adjusted EBITDA	$73,024	$66,252	$ 70,716

(a) Stock-based compensation expense represents non-cash expenses related to equity instruments granted to employees under our 2013 Performance Incentive Plan and Employee Stock Purchase Plan.

(b) Pre-opening expenses include expenses incurred in the preparation and opening of a new store location, such as payroll, travel and supplies, but do not include the cost of the initial inventory or capital expenditures required to open a location.

(c) As a result of the completion of our initial public offering and pursuant to the terms of the employment agreements with our executive officers, we paid $2.2 million in bonuses to our executive officers.

(d) Based on the court's most recent judgment in our favor regarding the Lacey Marketplace litigation, we determined that the likelihood of loss in this case is not probable, and, as such, we reversed the previous accrual of $4.0 million in our results for the fiscal year ended January 30, 2016. See Item 3. Legal Proceedings.

(e) We incurred certain costs related to our restructuring and emergence from Chapter 11 bankruptcy and included a liability as part of the reorganization value at August 14, 2009, the date of emergence from bankruptcy. Bankruptcy-related expenses are those amounts that are greater than the initial estimated restructuring costs. They are expensed as incurred.

(f) Acquisition expenses for fiscal year 2013 relate to the costs associated with the acquisition of our 10 previously operated stores in Montana, Oregon and Washington.

(g) Expenses paid by us in connection with a secondary offering of our common stock by affiliates of Seidler Equity Partners III, L.P. and one of our executive officers.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULS OF OPERATIONS

The discussion below contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those which are discussed in the "Risk Factors" section in Part I, Item 1A of this 10-K. Also see "Statement Regarding Forward-Looking Statements" preceding Part I.

The following discussion and analysis should be read in conjunction with the consolidated financial statements and the notes thereto included in this 10-K.

Overview

We are a high-growth outdoor sporting goods retailer focused on meeting the everyday needs of the seasoned outdoor veteran, the first-time participant and every enthusiast in between. Our mission is to provide a one-stop shopping experience that equips our customers with the right quality, brand name hunting, shooting, fishing and camping gear to maximize their enjoyment of the outdoors.

Our business was founded in 1986 as a single retail store in Midvale, Utah. Today, we operate 66 stores in 20 states, totaling approximately 2.8 million gross square feet. During fiscal year 2015, we increased our gross square footage by 9.8% through the opening of nine stores in the following locations:

Spokane, Washington on March 7, 2015;
Klamath Falls, Oregon on April 25, 2015;
Heber City, Utah on May 9, 2015;
Show Low, Arizona on June 27, 2015;
Williston, North Dakota on July 11, 2015;
Fresno, California on July 18, 2015;
Albany, Oregon on August 15, 2015;
Flagstaff, Arizona on September 12, 2015; and
Sheridan, Colorado on September 19, 2015.

During fiscal year 2016, we have opened stores in the following locations:

Slidell, Louisiana on February 27, 2016 and
South Jordan, Utah, on March 19, 2016.

Individual stores are aggregated into one operating and reportable segment.

How We Assess the Performance of Our Business

In assessing the performance of our business, we consider a variety of performance and financial measures. The key measures for determining how our business is performing are net sales, same store sales, gross margin, selling, general and administrative expenses, income from operations and Adjusted EBITDA.

Fiscal Year

We operate using a 52/53 week fiscal year ending on the Saturday closest to January 31. Fiscal years 2015, 2014 and 2013 ended on January 30, 2016, January 31, 2015 and February 1, 2014, respectively. Fiscal years 2015, 2014, and 2013 each contained 52 weeks of operations.

Net Sales and Same Store Sales

Our net sales are primarily received from revenue generated in our stores and also include sales generated through our e-commerce platform. When measuring revenue generated from our stores, we review our same store sales as well as the performance of our stores that have not operated for a sufficient amount of time to be included in same store sales. We include net sales from a store in same store sales on the first day of the 13th full fiscal month following the store's opening or acquisition by us. We exclude net sales from e-commerce from our calculation of same store sales.

Measuring the change in year-over-year same store sales allows us to evaluate how our retail store base is performing. Various factors affect same store sales, including:

- changes or anticipated changes to regulations related to some of the products we sell;
- consumer preferences, buying trends and overall economic trends;
- our ability to identify and respond effectively to local and regional trends and customer preferences;
- our ability to provide quality customer service that will increase our conversion of shoppers into paying customers;
- competition in the regional market of a store;
- atypical weather;
- changes in our product mix; and
- changes in pricing and average ticket sales.

Opening new stores is also an important part of our growth strategy. Since the beginning of fiscal year 2010, we opened 29 stores, including the nine new stores we have opened in fiscal year 2015 and the two new stores we have opened in fiscal year 2016. For the next several years, we intend to grow our store base at a rate of greater than 10 percent annually. As part of our growth strategy, we also re-acquired 10 stores in fiscal year 2013 that were previously operated under our Sportsman's Warehouse banner.

For our new locations, we measure our investment by reviewing the new store's four-wall Adjusted EBITDA margin and pre-tax return on invested capital ("ROIC"). We target a minimum 10% four-wall Adjusted EBITDA margin and a minimum ROIC of 50% excluding initial inventory costs (or 20% including initial inventory cost) for the first full twelve months of operation for a new store. The 20 new stores that we have opened since 2010 and that have been open for a full twelve months (excluding the 10 acquired stores) have achieved an average four-wall Adjusted EBITDA margin of 14.1% and an average ROIC of 98.3% excluding initial inventory cost (and 34.2% including initial inventory cost) during their first full twelve months of operations. Four-wall Adjusted EBITDA means, for any period, a particular store's Adjusted EBITDA, excluding any allocations of corporate selling, general and administrative expenses allocated to that store. Four-wall Adjusted EBITDA margin means, for any period, a store's four-wall Adjusted EBITDA divided by that store's net sales. For a definition of Adjusted EBITDA and Adjusted EBITDA margin and a reconciliation of net income to Adjusted EBITDA, see "—Non-GAAP Measures." ROIC means a store's four-wall Adjusted EBITDA for a given period divided by our initial cash investment in the store. We calculate ROIC both including and excluding the initial inventory cost.

We also have been scaling our e-commerce platform and increasing sales through our website, www.sportsmanswarehouse.com.

We believe the key drivers to increasing our total net sales will be:

- increasing our total gross square footage by opening new stores;
- continuing to increase and improve same store sales in our existing markets;
- increasing customer visits to our stores and improving our conversion rate through focused marketing efforts and continually high standards of customer service;
- increasing the average ticket sale per customer; and
- expanding our e-commerce platform.

Gross Profit

Gross profit is our net sales less cost of goods sold. Gross margin measures our gross profit as a percentage of net sales. Our cost of goods sold primarily consists of merchandise acquisition costs, including freight-in costs, shipping costs, payment term discounts received from the vendor and vendor allowances and rebates associated directly with merchandise and shipping costs related to e-commerce sales.

We believe the key drivers to improving our gross margin are increasing the product mix to higher margin products, particularly clothing and footwear, improving buying opportunities with our vendor partners and coordinating pricing strategies among our stores and buying group. Our ability to properly manage our inventory can also impact our gross profit. Successful inventory management ensures we have sufficient high margin products in stock at all times to meet customer demand, while overstocking of items could lead to markdowns in order to help a product sell. We believe that the overall growth of our business will allow us to generally maintain or increase our gross margins, because increased merchandise volumes will enable us to maintain our strong relationships with our vendors.

Selling, General and Administrative Expenses

We closely manage our selling, general and administrative expenses. Our selling, general and administrative expenses are comprised of payroll, rent and occupancy, depreciation and amortization, acquisition expenses, pre-opening expenses and other operating expenses, including share-based compensation expense and litigation accrual. Pre-opening expenses include expenses incurred in the preparation and opening of a new store location, such as payroll, travel and supplies, but do not include the cost of the initial inventory or capital expenditures required to open a location.

Our selling, general and administrative expenses are primarily influenced by the volume of net sales of our locations, except for our corporate payroll, rent and occupancy and depreciation and amortization, which are generally fixed in nature. We control our selling, general and administrative expenses through a budgeting and reporting process that allows our personnel to adjust our expenses as trends in net sales activity are identified.

We expect that our selling, general and administrative expenses will increase in future periods due to our continuing growth and in part to additional legal, accounting, insurance and other expenses we expect to incur as a result of being a public company.

Income from Operations

Income from operations is gross profit less selling, general and administrative expenses. We use income from operations as an indicator of the productivity of our business and our ability to manage selling, general and administrative expenses.

Adjusted EBITDA

We define Adjusted EBITDA as net income plus interest expense, income tax expense, depreciation and amortization, stock-based compensation expense, pre-opening expenses, and other gains, losses, and expenses that we do not believe are indicative of our ongoing expenses. In evaluating our business, we use Adjusted EBITDA and Adjusted EBITDA margin as an additional measurement tool for purposes of business decision-making, including evaluating store performance, developing budgets and managing expenditures. See “—Non-GAAP Measures.”

Results of Operations

The following table summarizes key components of our results of operations as a percentage of net sales for the periods indicated:

	Fiscal Year Ended		
	January 30, 2016	January 31, 2015	February 1, 2014

Percentage of net sales:						
Net sales	100.0	%	100.0	%	100.0	%
Cost of goods sold	67.3		67.4		67.8	
Gross profit	32.7		32.6		32.2	
Selling, general and administrative expenses	24.6		25.8		22.9	
Bankruptcy-related expenses	0.0		0.0		0.0	
Income from operations	8.1		6.8		9.3	
Interest expense	1.9		3.4		3.9	
Income before income taxes	6.2		3.4		5.4	
Income tax expense	2.4		1.3		2.0	
Net income	3.8	%	2.1	%	3.4	%
Adjusted EBITDA	10.0	%	10.0	%	10.9	%

The following table shows our sales during the periods presented by department:

		Fiscal Year Ended		
Department	Product Offerings	January 30, 2016	January 31, 2015	February 1, 2014
Camping	Backpacks, camp essentials, canoes and kayaks, coolers, outdoor cooking equipment, sleeping bags, tents and tools	14.2 %	13.5 %	12.1 %
Clothing	Camouflage, jackets, hats, outerwear, sportswear, technical gear and work wear	8.6	9.5	8.8
Fishing	Bait, electronics, fishing rods, flotation items, fly fishing, lines, lures, reels, tackle and small boats	9.6	9.5	8.8
Footwear	Hiking boots, socks, sport sandals, technical footwear, trail shoes, casual shoes, waders and work boots	7.1	7.4	6.6
Hunting and Shooting	Ammunition, archery items, ATV accessories, blinds and tree stands, decoys, firearms, reloading equipment and shooting gear	48.6	47.9	52.1
Optics, Electronics and Accessories	Gift items, GPS devices, knives, lighting, optics (e.g. binoculars) and two-way radios	9.3	9.5	9.1
Other		2.6	2.7	2.5
Total		100.0 %	100.0 %	100.0 %

Fiscal Year 2015 Compared to Fiscal Year 2014

Net Sales. Net sales increased by $69.9 million, or 10.6%, to $729.9 million in the fiscal year 2015 compared to $660.0 million in fiscal year 2014. Net sales increased due to net sales generated from our nine new stores openings during fiscal year 2015 and a full year of the eight stores opened during fiscal year 2014 for the period of time prior to inclusion in our same store sales. These new stores generated $62.5 million in additional net sales in the fiscal year 2015 compared to fiscal year 2014. This increase from our new store openings was supplemented by an increase in our same stores sales for the period of 1.1%.

With respect to same store sales, three of our six departments (camping, hunting and shooting, and fishing) realized an increase in same store sales. Our hunting and shooting department experienced a same store sales increase of 2.2% during fiscal year 2015 when compared to fiscal year 2014. Our camping and fishing departments experienced same store sales increases of 6.5% and 2.6%, respectively. Sales in our camping department were positively impacted by increased product innovations within various categories. The increases in camping, hunting and shooting, and fishing were partially offset by the clothing, footwear, and optics, electronics and accessories departments, which had same store sales decreases of 7.7%, 2.3%, and 1.0%, respectively, during the same period. Our clothing and footwear departments were negatively impacted by unseasonably warm weather in the majority of our markets. As of January 30, 2016, we had 55 stores included in our same store sales calculation.

During fiscal year 2015, we opened nine new stores. These nine new locations generated net sales of $47.1 million during this period. Existing stores that were not included in same store sales generated $15.4 million in additional net sales in fiscal year 2015 over fiscal year 2014.

Net sales from our e-commerce business increased by $0.2 million, or 2.7%, to $7.7 million in fiscal year 2015 compared to $7.5 million in fiscal year 2014.

Gross Profit. Gross profit increased by $23.3 million, or 10.8%, to $238.5 million for fiscal year 2015 from $215.2 million for fiscal year 2014. As a percentage of net sales, gross profit increased by 0.1% to 32.7% for fiscal year 2015 from 32.6% in fiscal year 2014. The increase in gross profit from the prior fiscal year was due to an increase in vendor incentives received during the year.

Selling, General and Administrative Expenses. Selling, general and administrative expenses increased by $8.9 million, or 5.2%, to $179.2 million for fiscal year 2015 from $170.3 million for fiscal year 2014. Selling, general and administrative expenses were 24.6% of net sales in fiscal year 2015 compared to 25.8% of net sales in fiscal year 2014. In fiscal year 2015, we incurred $0.7 million in costs related to a secondary offering. Also, in fiscal year 2015, we reversed the $4.0 million accrual taken in fiscal year 2014 related to the Lacey Marketplace litigation matter because the court granted our motion for judgment as a matter of law. In fiscal year 2014, we paid a one-time discretionary bonus of $2.2 million in conjunction with the successful completion of our initial public offering. We did not incur this expense in fiscal year 2015. Excluding the secondary offering costs, the litigation accrual and subsequent reversal, and the one-time bonus, selling, general and administrative expenses increased by $18.4 million and selling, general and administrative expenses were 25.0% of net sales in fiscal year 2015 compared to 24.9% of net sales in fiscal year 2014. Specifically, we incurred additional payroll, rent, and depreciation and amortization of $7.1 million, $3.2 million, and $2.4 million, respectively, during fiscal year 2015 compared to fiscal year 2014, but these increases were lower on a per-store percentage basis. We also incurred additional operating expenses of $5.2 million in fiscal year 2015 related to an increase in professional fees and other fees related to the Lacey Marketplace litigation matter as well as fees incurred as part of the additional stores that opened during the year.

Interest Expense. Interest expense decreased by $8.3 million, or 37.0%, to $14.2 million in fiscal year 2015 from $22.5 million for fiscal year 2014. Interest expense decreased primarily as a result of our lower debt balance and lower interest rate on the debt during fiscal year 2015 compared to fiscal year 2014 as a result of the refinance on our term loan in December 2014 and the amendment on our line of credit facility in August 2015.

Income Taxes. We recorded an income tax expense of $17.4 million for fiscal year 2015 compared to income tax expense of $8.6 million for fiscal year 2014. Our effective tax rate remained unchanged in fiscal year 2015 from fiscal year 2014 at 38.5%. The effective tax rate did not change as there were no material legislative changes impacted the state tax rate or state apportionment methods in certain states where we operate.

Fiscal Year 2014 Compared to Fiscal Year 2013

Net Sales. Net sales increased by $16.8 million, or 2.6%, to $660.0 million in the fiscal year 2014 compared to $643.2 million in fiscal year 2013. Net sales increased due to net sales generated from our eight new stores openings during fiscal year 2014 and a full year of the 14 stores, either opened or acquired, during fiscal year 2013 for the period of time prior to inclusion in our same store sales. These new stores generated $69.5 million in additional net sales in the fiscal year 2014 compared to fiscal year 2013. This increase from our new store openings was partially offset by a decline in our same stores sales for the period of 8.4% (or a decrease of 2.5% excluding firearms and ammunition).

Each of our departments recognized an increase in net sales in fiscal year 2014 from fiscal year 2013 except for our hunting and shooting department. Our camping, clothing, fishing, footwear and optics, electronics and accessories departments had a combined increase of $32.4 million in net sales over the prior year period as a result of the expansion of our product offerings in the clothing and footwear departments that was a result of the roll out of a "store-within-a-store" concept with certain of our key vendors and increased demand in our camping department. This increase was partially offset by an $18.3 million decrease in the hunting and shooting department as a result of decreased demand for firearms, ammunition and related products as compared to the corresponding period of fiscal year 2013. During the fourth fiscal quarter of fiscal year 2012, we experienced increased demand for firearms that continued into fiscal year 2013, due in part to the public perception during that period that federal or state legislation might be enacted that would potentially make it more difficult to purchase certain firearms, ammunition and reloading supplies. Our sales of firearms returned closer to historical sales levels during the latter part of fiscal year 2013, which when combined with sales of ammunition and related products, resulted in the decrease in same store sales for fiscal year 2014 compared to the same period in fiscal year 2013.

With respect to same store sales, four of our six departments (clothing, hunting and shooting, fishing, and optics, electronics and accessories) realized a decline in same store sales because of the decrease in demand for firearms and ammunition, as discussed above, and the associated decrease in customer traffic associated with this decreased demand. Our hunting and shooting department experienced a same store sales decline of 16.1% during fiscal year 2014 when compared to fiscal year 2013. Warm weather in our markets also adversely impacted the sales of our clothing products causing clothing department sales to decline approximately 2.0% when compared with clothing department sales from fiscal year 2013. These declines were partially offset by the camping and footwear departments, which had same store sales increases of 2.9% and 3.3%, respectively, during the same period. As of January 31, 2015, we had 47 stores included in our same store sales calculation.

During fiscal year 2014, we opened eight new stores. These eight new locations generated net sales of $51.1 million during this period. Existing stores that were not included in same store sales generated $18.4 million in additional net sales in fiscal year 2014 over fiscal year 2013.

Net sales from our e-commerce business remained flat at $7.5 million in fiscal year 2014 when compared to fiscal year 2013.

Gross Profit. Gross profit increased by $8.0 million, or 3.8%, to $215.2 million for fiscal year 2014 from $207.2 million for fiscal year 2013. As a percentage of net sales, gross profit increased by 0.4% to 32.6% for fiscal year 2014 from 32.2% in fiscal year 2013. The increase in gross profit from the corresponding period of the prior fiscal year was due to an increase in vendor incentives received during the year combined with a shift in the sales mix from lower margin products to higher margin products.

Selling, General and Administrative Expenses. Selling, general and administrative expenses increased by $23.2 million, or 15.8%, to $170.3 million for fiscal year 2014 from $147.1 million for fiscal year 2013. The increase in these expenses resulted from an increase in the number of stores in operation over the corresponding period of the prior year. Our payroll, rent and depreciation and amortization expenses increased $10.7 million, $4.7 million and $2.9 million, respectively, for fiscal year 2014 from fiscal year 2013. Also, as described in "Item 3. Legal Proceedings", there was an additional $4.0 million increase in other operating expenses due to an accrual with respect to a litigation matter. These increases were partially offset by a decrease in the costs associated with our acquisition of the 10 stores in March 2013 of $2.3 million during fiscal year 2013. Our total payroll expense for the first half of fiscal year 2014 included $2.2 million in bonuses paid as a result of the successful completion of our initial public offering and pursuant to the terms of the employment agreements with our executive officers and $3.3 million in non-cash stock-based compensation, $1.2 million of which was due to accelerated vesting triggered by our initial public offering. Selling, general and administrative expenses were 25.8% of net sales in fiscal year 2014 compared to 22.9% of net sales in fiscal year 2013. Selling, general and administrative expenses increased as a percentage of net sales primarily due to the increase in bonuses and stock-based compensation expense related to our initial public offering, increased payroll, rent and pre-opening expenses from the new store locations and the litigation accrual described above.

Interest Expense. Interest expense decreased by $3.0 million, or 11.7%, to $22.5 million in fiscal year 2014 from $25.4 million for fiscal year 2013. Interest expense decreased primarily as a result of our lower debt balance during fiscal year 2014 compared to fiscal year 2013. Specifically, as described below under "—Liquidity and Capital Resources," we used the net proceeds from our initial public offering and partial exercise of the underwriter's overallotment to repay $73.3 million outstanding under our term loan facility in April and May of 2014. Additionally, we refinanced our term loan in the fourth quarter of 2014, which resulted in additional interest expense of $5.7 million in fiscal year 2014 related to this refinance and increased our outstanding amount from $158.8 million to $160.0 million. In August 2013, we refinanced our term loan facility and increased the outstanding amount under this facility by $110.0 million, from $125.0 million to $235.0 million, and, as a result of this refinance, we recorded $8.1 million of interest expense in fiscal year 2013.

Income Taxes. We recorded an income tax expense of $8.6 million for fiscal year 2014 compared to income tax expense of $12.8 million for fiscal year 2013. Our effective tax rate for fiscal year 2014 of 38.5% increased from the effective tax rate for fiscal year 2013 of 37.1%. The increase was primarily due to legislative changes which impacted the apportionment methods in certain states where we operate.

Seasonality

Due to holiday buying patterns and the openings of hunting season across the country, net sales are typically higher in the third and fourth fiscal quarters than in the first and second fiscal quarters. We also incur additional expenses in the third and fourth fiscal quarters due to higher volume and increased staffing in our stores. We anticipate our net sales will continue to reflect this seasonal pattern.

The timing of our new retail store openings also may have an impact on our quarterly results. First, we incur certain one-time expenses related to opening each new retail store, all of which are expensed as they are incurred. Second, most store expenses generally vary proportionately with net sales, but there is also a fixed cost component, which includes occupancy costs. These fixed costs typically result in lower store profitability during the initial period after a new retail store opens. Due to both of these factors, new retail store openings may result in a temporary decline in operating profit, in dollars and/or as a percentage of net sales.

Weather conditions affect outdoor activities and the demand for related clothing and equipment. Customers' demand for our products, and, therefore, our net sales, can be significantly impacted by weather patterns on a local, regional and national basis.

Quarterly Results of Operations

The following table sets forth unaudited financial and operating data for each fiscal quarter of fiscal years 2015 and 2014. This quarterly information has been prepared on a basis consistent with our audited financial statements and includes all normal recurring adjustments that we consider necessary for a fair presentation of the information shown. This information should be read in conjunction with "Part II, Item 6. Selected Financial Data" and "Part II, Item 8. Financial Statements and Supplementary Data" of this 10-K. Our quarterly operating results may fluctuate significantly as a result of the factors described above and a variety of other factors, and operating results for any fiscal quarter are not necessarily indicative of results for a full fiscal year.

	Fiscal Year 2015				Fiscal Year 2014			
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
	(unaudited)							
	(in thousands, except per share data, percentages and number of stores)							
Net sales	$212,730	$199,704	$172,985	$144,493	$185,578	$182,532	$159,468	$132,425
Gross profit	70,812	66,565	58,002	43,151	61,601	60,651	52,827	40,128
Income (loss) from operations (1)	22,109	19,169	16,786	1,248	14,145	18,625	12,343	(221)
Net income (loss) (1)(2)	11,390	9,541	8,200	(1,360)	3,173	8,916	5,063	(3,368)
Diluted earnings (loss) per share	0.27	0.23	0.19	(0.03)	0.08	0.21	0.12	(0.10)
As a percentage of full year results:								
Net sales	29.1 %	27.4 %	23.7 %	19.8 %	28.1 %	27.7 %	24.2 %	20.0 %
Gross profit	29.7	27.9	24.3	18.1	28.6	28.2	24.6	18.6
Income (loss) from operations	37.3	32.3	28.3	2.1	31.4	41.3	27.5	(0.5)
Net income (loss)	41.0	34.4	29.5	(4.9)	18.5	52.0	29.5	(20.7)
Operating data:								
Number of stores open at end of period	64	64	61	57	55	55	54	51

(1) This line includes, for the third quarter of 2015, $0.7 million in expenses paid by us in connection with a secondary offering of our common stock by affiliates of Seidler Equity Partners III, L.P. and one of our executive officers; for the fourth quarter of fiscal year 2014, an accrual of $4.0 million and, for the second quarter of fiscal year 2015, the reversal of the $4.0 million accrual, with respect to the litigation matter discussed in the "Legal Matters" subsection of Note 17 to our consolidated financial statements; and, for the first quarter of 2014, $2.2 million in bonuses that

were paid to our executive officers as a result of the completion of our initial public offering and pursuant to the terms of the employment agreements with our executive officers.

(2) Includes, for the fourth quarter of fiscal year 2014, term loan refinance-related fees of $5.7 million.

Liquidity and Capital Resources

Our primary capital requirements are for seasonal working capital needs and capital expenditures related to opening new stores. Our sources of liquidity to meet these needs have primarily been borrowings under our revolving credit facility, operating cash flows and short and long-term debt financings from banks and financial institutions. We believe that our cash on hand, cash generated by operating activities and funds available under our revolving credit facility will be sufficient to finance our operating activities for at least the next twelve months.

For fiscal year 2015, we incurred approximately $34.0 million in gross capital expenditures. We also received $19.0 million from sale-leaseback transactions. We expect gross capital expenditures between $35.0 million and $40.0 million for fiscal year 2016. We intend to fund these initiatives with our operating cash flows and funds available under our revolving credit facility. Other investment opportunities, such as potential strategic acquisitions or store expansion rates in excess of those presently planned, may require additional funding.

Cash flows from operating, investing and financing activities are shown in the following table:

	Fiscal Year Ended	
	January 30, 2016	January 31, 2015
	(in thousands)	
Cash flows from operating activities	$35,662	$20,473
Cash flows from investing activities	(14,951)	(30,167)
Cash flows from financing activities	(20,353)	10,091
Cash and cash equivalents at end of period	2,109	1,751

Net cash provided by operating activities was $35.7 million for fiscal year 2015, compared to $20.5 million for fiscal year 2014. Our net cash provided by operating activities increased primarily due to favorable changes in accounts payable, income taxes receivable and payable, deferred income taxes, and depreciation of $17.4 million, $8.9 million, $3.1 million, and $2.4 million, respectively, as well as a $14.0 million increase in net income compared to fiscal year 2014. These increases were partially offset by unfavorable changes in inventory, accrued expenses, amortization of discount on debt and deferred financing fees, prepaid expenses, and deferred rent of $7.3 million, $7.1 million, $5.7 million, $5.5 million, and $4.2 million, respectively.

Net cash used in investing activities was $15.0 million for fiscal year 2015 compared to $30.2 million for fiscal year 2014. The decrease in cash used in investing activities was primarily a result of proceeds of $19.0 million received from sale-leaseback transactions in fiscal year 2015. Capital expenditures increased by $3.8 million to $34.0 million for fiscal year 2015 compared to $30.2 million for fiscal year 2014. This increase was primarily a result of opening one additional store in fiscal year 2015 compared to fiscal year 2014.

Net cash used in financing activities was $20.4 million for fiscal year 2015 compared to net cash provided by financing activities of $10.1 million for fiscal year 2014. In fiscal year 2015, net cash used in financing activities was primarily for $18.2 million in repayments on our revolving line of credit and term loan. In contrast, in fiscal year 2014, we received net proceeds of $12.0 million from our initial public offering and borrowings under our term loan and revolving line of credit, net of repayments on our outstanding debt. Our outstanding debt consists of our senior secured revolving line of credit and our senior secured term loans.

Senior Secured Revolving Credit Facility. We have a senior secured revolving credit facility with Wells Fargo Bank, National Association, or Wells Fargo, that provides for borrowings in the aggregate amount of up to $135.0 million, subject to a borrowing base calculation. As of January 30, 2016, $89.5 million was available for borrowing and $25.3 million was outstanding under the revolving credit facility. All borrowings under the revolving credit facility are limited to a borrowing base equal to roughly (1) the lesser of (a) 90% of the net orderly liquidation value of our eligible inventory and (b) 75% of the lower of cost or market value of our eligible inventory, plus (2) 90% of the eligible accounts receivable, less certain reserves against outstanding gift cards, layaway deposits and amounts outstanding under commercial letters of credit, each term as defined in the credit agreement. The revolving credit facility matures on December 3, 2019.

Each of the subsidiaries of Sportsman’s Warehouse Holdings, Inc., or Holdings, is a borrower under the revolving credit facility, and all obligations under the revolving credit facility are guaranteed by Holdings. All of our obligations under the revolving credit facility are secured by a lien on substantially all of Holdings’ tangible and intangible assets and the tangible and intangible assets of all of our subsidiaries, including a pledge of all capital stock of each of our subsidiaries. The lien securing the obligations under the revolving credit facility is a first priority lien as to certain liquid assets, including cash, accounts receivable, deposit accounts and inventory. In addition, the credit agreement contains provisions that enable Wells Fargo to require us to maintain a lock-box for the collection of all receipts.

Borrowings under the revolving credit facility bear interest based on either, at our option, the base rate or LIBOR, in each case plus an applicable margin. The base rate is the higher of (1) Wells Fargo’s prime rate, (2) the federal funds rate (as defined in the credit agreement) plus 0.50% and (3) the one-month LIBOR (as defined in the credit agreement) plus 1.00%. The applicable margin for loans under the revolving credit facility, which varies based on the average daily availability, ranges from 0.50% to 1.00% per year for base rate loans and from 1.50% to 2.00% per year for LIBOR loans. The weighted average interest rate on the amount outstanding under the revolving credit facility as of January 30, 2016 was 2.16%.

Interest on base rate loans is payable monthly in arrears and interest on LIBOR loans is payable based on the LIBOR interest period selected by us, which can be 30, 60 or 90 days. All amounts that are not paid when due under our revolving credit facility will accrue interest at the rate otherwise applicable plus 1.75% until such amounts are paid in full.

We may be required to make mandatory prepayments under the revolving credit facility in the event of a disposition of certain property or assets, in the event of receipt of certain insurance or condemnation proceeds, upon the issuance of certain debt or equity securities, upon the incurrence of certain indebtedness for borrowed money or upon the receipt of certain payments not received in the ordinary course of business.

The revolving credit facility contains customary affirmative and negative covenants, including covenants that limit our ability to incur, create or assume certain indebtedness, to create, incur or assume certain liens, to make certain investments, to make sales, transfers and dispositions of certain property and to undergo certain fundamental changes, including certain mergers, liquidations and consolidations. The revolving credit facility also requires us to maintain a minimum availability at all times of not less than 10% of the gross borrowing base, and in any event, not less than $5.0 million. The revolving credit facility also contains customary events of default. As of January 30, 2016, we were in compliance with all covenants under the revolving credit facility.

Senior Secured Term Loan. We have a $160.0 million senior secured term loan facility with a financial institution. The term loan was issued at a price of 99% of the aggregate principal amount and has a maturity date of December 3, 2020. The term loan requires quarterly principal payments of $0.4 million payable on the last business day of each fiscal quarter continuing up to and including October 30, 2020. A final installment payment consisting of the remaining unpaid balance is due on December 3, 2020. As of January 30, 2016, there was $158.0 million outstanding under the term loan.

All of Sportsman’s Warehouse, Inc.’s obligations under the term loan are guaranteed by Holdings, Minnesota Merchandising Corporation, a wholly owned subsidiary of Holdings, and each of Sportsman’s Warehouse, Inc.’s subsidiaries.

The term loan is secured by a lien on substantially all of the tangible and intangible assets of Sportsman’s Warehouse, Inc. The lien securing the obligations under the term loan is a first priority lien as to certain non-liquid assets, including equipment, intellectual property, proceeds of assets sales and other personal property.

Sportsman’s Warehouse, Inc. may be required to make mandatory prepayments on the term loan in the event of, among other things, certain asset sales, the receipt of payment in respect of certain insurance claims or upon the issuance or incurrence of certain indebtedness. Sportsman’s Warehouse, Inc. may also be required to make mandatory prepayments based on any excess cash flows as defined in the term loan agreement. Due to our profitability during fiscal year 2015, we are required to make a mandatory prepayment of approximately $7.7 million by May 6, 2016, which will reduce the amount outstanding under the term loan.

The term loan bears interest at a rate per annum equal to the one-, two-, three-, or six-month LIBOR (or, the nine- or 12-month LIBOR), as defined in the term loan agreement, at our election, which cannot be less than 1.25%, plus an applicable margin of 6.00%.

The term loan contains customary affirmative and negative covenants, including covenants that limit our ability to incur, create or assume certain indebtedness, to incur or assume certain liens, to purchase, hold or acquire certain investments, to declare or make certain dividends and distributions and to engage in certain mergers, consolidations and asset sales. The term loan also requires us to comply with specified financial covenants, including a minimum interest coverage ratio and a maximum total net leverage ratio. The term loan also contains customary events of default. As of January 30, 2016, we were in compliance with all covenants under the term loan.

Critical Accounting Policies

Our financial statements are prepared in accordance with GAAP. In connection with the preparation of the financial statements, we are required to make assumptions, make estimates and apply judgment that affect the reported amounts of assets, liabilities, revenue, expenses and the related disclosures. We base our assumptions, estimates and judgments on historical experience, current trends and other factors that we believe to be relevant at the time the consolidated financial statements are prepared. On a regular basis, we review the accounting policies, assumptions, estimates and judgments to ensure that our financial statements are presented fairly and in accordance with GAAP. However, because future events and their effects cannot be determined with certainty, actual results could differ from our assumptions and estimates, and such differences could be material.

Our significant accounting policies are discussed in Note 2 of the Notes to our consolidated financial statements. We believe that the following accounting policies are the most critical to aid in fully understanding and evaluating our reported financial results.

Revenue Recognition

We recognize revenue on our retail sales at the time of the sale in the store. We record a reserve for estimated product returns in each reporting period based on our historical experience. Had our estimate of product returns been lower or higher by 10% as of January 30, 2016, our operating income would have been correspondingly higher or lower by approximately $0.1 million.

Our policy regarding gift cards sold is to record revenue as the gift cards are redeemed for merchandise. Prior to their redemption, the gift cards are recorded as a liability. Gift card breakage income is recognized based upon historical redemption patterns and represents the balance of gift cards for which we believe the likelihood of redemption by the customer is remote. During the fiscal years ended January 30, 2016 and January 31, 2015, we recognized $0.8 million and $0.8 million, respectively, in gift card breakage income. We include gift card breakage income as a reduction in selling, general and administrative expenses, if applicable. Had our estimate of breakage on our recorded liability for gift cards been lower or higher by 10% of the recorded liability as of January 30, 2016, our selling, general and administrative expenses would have been correspondingly higher or lower by approximately $0.9 million.

Loyalty breakage income is recognized based upon the balance of loyalty points that have expired after a dormancy period of 18 months. During the fiscal year ended January 30, 2016, we recognized $0.2 million of loyalty breakage income. We did not recognize any loyalty breakage income for the fiscal year ended January 31, 2015. This income is included in the accompanying consolidated statements of income as an increase in net sales. Had our estimate of breakage on our recorded liability for loyalty points been lower or higher by 10% of the recorded liability as of January 30, 2016, our net sales would have been correspondingly higher or lower by less than $0.1 million.

Inventory Valuation

We value our inventory at the lower of cost or market. Cost is determined using the weighted average cost method. We estimate a provision for inventory shrinkage based on our historical inventory accuracy rates as determined by periodic cycle counts. The allowance for damaged goods from returns is based upon our historical experience. We also adjust inventory for obsolete or slow moving inventory based on inventory productivity reports and by specific identification of obsolete or slow moving inventory. Had our estimated inventory reserves been lower or higher by 10% as of January 30, 2016, our cost of sales would have been correspondingly lower or higher by approximately $0.4 million.

Valuation of Long-Lived Assets

We review our long-lived assets with definite lives for impairment whenever events or changes in circumstances may indicate that the carrying value of an asset may not be recoverable. We use an estimate of the future undiscounted net cash flows of the related asset or group of assets over their remaining useful lives in measuring whether the assets are recoverable. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized for the amount by which the carrying amount exceeds the estimated fair value of the asset. Impairment of long-lived assets is assessed at the lowest levels for which there are identifiable cash flows that are independent of other groups of assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value, less the estimated costs to sell. No impairment charge to long-lived assets was recorded during the fiscal year ended January 30, 2016 or January 31, 2015.

Off Balance Sheet Arrangements

We are not party to any off balance sheet arrangements.

Contractual Obligations

The following table summarizes our contractual obligations as of January 30, 2016 and the effect such obligations are expected to have on our liquidity and cash flows in future periods.

Payments Due by Period

	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
	(in thousands)				
Long-term debt obligations (1)	$210,317	$20,415	$24,796	$165,106	$—
Operating lease obligations (2)	295,704	36,840	75,277	68,990	114,597
Standby letters of credit	750	750	—	—	—
Purchase obligations (3)	13,471	13,236	217	18	—

(1) Long-term debt obligations do not reflect the amounts outstanding under our revolving credit facility, because those amounts are considered current liabilities, and do not reflect any mandatory prepayments of our term loans that may be required upon the occurrence of certain events, which are described above under "—Liquidity and Capital Resources." Long-term obligations include interest to be paid until maturity. For loans that have variable rate interest, we have calculated future interest obligations based on the interest rate for that loan as of January 30, 2016.

(2) Operating lease obligations in the table above do not include additional payments associated with common area maintenance, real estate, taxes and insurance. Such payments were $7.3 million, $6.3 million and $5.0 million in fiscal years 2015, 2014, and 2013, respectively.

(3) In the ordinary course of business, we enter into arrangements with vendors to purchase merchandise in advance of expected delivery. Because these purchase orders do not contain any termination payments or other penalties if cancelled, they are not included in this table of contractual obligations. In accordance with GAAP, these obligations are not recorded in our financial statements.

Non-GAAP Measures

In evaluating our business, we use Adjusted EBITDA and Adjusted EBITDA margin as supplemental measures of our operating performance. We define Adjusted EBITDA as net income plus interest expense, income tax expense, depreciation and amortization, stock-based compensation expense, pre-opening expenses, and other gains/losses, and expenses that we do not believe are indicative of our ongoing expenses. Adjusted EBITDA margin means, for any period, the Adjusted EBITDA for that period divided by the net sales for that period. We consider Adjusted EBITDA and Adjusted EBITDA margin important supplemental measures of our operating performance and believe they are frequently used by analysts, investors and other interested parties in the evaluation of companies in our industry. Other companies in our industry, however, may calculate Adjusted EBITDA and Adjusted EBITDA margin differently than we do. Management also uses Adjusted EBITDA and Adjusted EBITDA margin as additional measurement tools for purposes of business decision-making, including evaluating store performance, developing budgets and managing expenditures.

Adjusted EBITDA is not defined under GAAP and is not a measure of operating income, operating performance or liquidity presented in accordance with GAAP. Adjusted EBITDA has limitations as an analytical tool, and when assessing our operating performance, you should not consider Adjusted EBITDA in isolation or as a substitute for net income or other consolidated income statement data prepared in accordance with GAAP. Some of these limitations include, but are not limited to:

- Adjusted EBITDA does not reflect our cash expenditures or future requirements for capital expenditures or contractual commitments;
- Adjusted EBITDA does not reflect changes in, or cash requirements for, our working capital needs;
- Adjusted EBITDA may be defined differently by other companies, and, therefore, it may not be directly comparable to the results of other companies in our industry;
- Adjusted EBITDA does not reflect the interest expense, or the cash requirements necessary to service interest or principal payments, on our debt; and
- Adjusted EBITDA does not reflect income taxes or the cash requirements for any tax payments.

The following table presents a reconciliation of net income, the most directly comparable financial measure presented in accordance with GAAP, to Adjusted EBITDA for the fiscal years ended January 30, 2016, January 31, 2015, and February 1, 2014.

	Fiscal Year Ended		
	January 30, 2016	January 31, 2015	February 1, 2014
	(dollars in thousands)		
Net income	$27,771	$13,784	$21,750
Plus:			
Interest expense	14,156	22,480	25,447
Income tax expense	17,385	8,628	12,838
Depreciation and amortization	11,569	9,150	6,277
Stock-based compensation expense (1)	2,257	3,293	365
Pre-opening expenses (2)	3,159	2,717	1,653
IPO bonus (3)	—	2,200	—
Litigation accrual (reversal) (4)	(4,000)	4,000	—
Bankruptcy-related expenses (5)	—	—	55
Acquisition expenses (6)	—	—	2,331
Secondary offering expenses (7)	727	—	—
Adjusted EBITDA	$73,024	$66,252	$70,716
Adjusted EBITDA margin	10.0 %	10.0 %	10.9 %

(1) Stock-based compensation expense represents non-cash expenses related to equity instruments granted to employees under our 2013 Performance Incentive Plan and Employee Stock Purchase Plan.

(2) Pre-opening expenses include expenses incurred in the preparation and opening of a new store location, such as payroll, travel and supplies, but do not include the cost of the initial inventory or capital expenditures required to open a location.

(3) As a result of the completion of our initial public offering and pursuant to the terms of the employment agreements with our executive officers, we paid $2.2 million in bonuses to our executive officers.

(4) Based on the court's most recent judgment in our favor regarding the Lacey Marketplace litigation, we determined that the likelihood of loss in this case is not probable, and, as such, we reversed the previous accrual of $4.0 million in our results for the fiscal year ended January 30, 2016. See Item 3. Legal Proceedings.

(5) We incurred certain costs related to our restructuring and emergence from Chapter 11 bankruptcy and included a liability as part of the reorganization value at August 14, 2009, the date of emergence from bankruptcy. Bankruptcy-related expenses are those amounts that are greater than the initial estimated restructuring costs. They are expensed as incurred.

(6) Acquisition expenses for fiscal year 2013 relate to the costs associated with the acquisition of our 10 previously operated stores in Montana, Oregon and Washington.

(7) Expenses paid by us in connection with a secondary offering of our common stock by affiliates of Seidler Equity Partners III, L.P. and one of our executive officers.

Recent Accounting Pronouncements

For a description of recent accounting pronouncements, see the notes to our consolidated financial statements. Under the Jumpstart Our Business Startup Act, "emerging growth companies" ("EGCs") can delay adopting new or revised accounting standards until such time as those standards apply to private companies. We have irrevocably elected not to avail ourselves of this exemption from new or revised accounting standards, and, therefore, we will be subject to the same new or revised accounting standards as other public companies that are not EGCs.

We will continue to be an EGC for a period up to the end of the fifth fiscal year after our initial public offering. We could cease to be an EGC earlier than this five-year period if our total annual gross revenues equal or exceed $1 billion in a fiscal year, if we issue more than $1 billion in non-convertible debt over a three-year period or if we become a "large accelerated filer" (which requires, among other things, the market value of our common stock held by non-affiliates to be at least $700 million as of the last business day of our second fiscal quarter of any fiscal year). For further information, see Part I, Item 1A. "Risk Factors—We are an EGC within the meaning of the JOBS Act and we cannot be certain if the reduced reporting requirements applicable to EGCs will make our common stock less attractive to investors."

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our principal exposure to market risk relates to changes in interest rates. Our revolving credit facility and term loans carry floating interest rates that are tied to LIBOR, the federal funds rate and the prime rate, and, therefore, our income and cash flows will be exposed to changes in interest rates to the extent that we do not have effective hedging arrangements in place. We historically have not used interest rate swap agreements to hedge the variable cash flows associated with the interest on our credit facilities. At January 30, 2016, the weighted average interest rate on our borrowings under our revolving credit facility was 2.16%. Based on a sensitivity analysis at January 30, 2016, assuming the amount outstanding under our revolving credit facility would be outstanding for a full year, a 100 basis point increase in interest rates would increase our annual interest expense by approximately $0.3 million. As long as LIBOR is less than 1.25%, the interest rate on our $160.0 million term loan will be fixed at 7.25%. Since we entered into the term loan facility on December 3, 2014, LIBOR has not exceeded 1.25%. We do not use derivative financial instruments for speculative or trading purposes. However, this does not preclude our adoption of specific hedging strategies in the future.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders

Sportsman’s Warehouse Holdings, Inc.:

We have audited the accompanying consolidated balance sheets of Sportsman’s Warehouse Holdings, Inc. and subsidiaries as of January 30, 2016 and January 31, 2015, and the related consolidated statements of income, stockholders’ deficit, and cash flows for each of the fiscal years in the three-year period ended January 30, 2016. These consolidated financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Sportsman’s Warehouse Holdings, Inc. and subsidiaries as of January 30, 2016 and January 31, 2015, and the results of their operations and their cash flows for each of the fiscal years in the three-year period ended January 30, 2016, in conformity with U.S. generally accepted accounting principles.

/s/ KPMG LLP

Salt Lake City, Utah

March 24, 2016

SPORTSMAN'S WAREHOUSE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

Amounts in Thousands, Except Per Share Data

	January 30, 2016	January 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	$2,109	$1,751
Accounts receivable, net	469	425
Merchandise inventories	217,794	185,909
Prepaid expenses and other	9,686	7,468
Deferred income taxes, current	3,001	2,928
Income taxes receivable	—	5,190
Total current assets	233,059	203,671
Property and equipment, net	62,432	54,317
Deferred income taxes, noncurrent	2,263	5,398
Definite lived intangibles, net	3,923	5,729
Other long-term assets, net	1,347	1,608
Total assets	$303,024	$270,723
Liabilities and Stockholders' Deficit		
Current liabilities:		
Accounts payable	$46,698	$28,500
Accrued expenses	42,480	42,620
Income taxes payable	1,779	—
Revolving line of credit	25,263	41,899
Current portion of long-term debt, net of discount	9,033	1,333
Current portion of deferred rent	3,018	2,873
Total current liabilities	128,271	117,225
Long-term liabilities:		
Long-term debt, net of discount and current portion	147,679	156,713
Deferred rent, noncurrent	29,133	28,117
Total long-term liabilities	176,812	184,830
Total liabilities	305,083	302,055
Commitments and contingencies		
Stockholders' deficit:		
Preferred stock, $.01 par value; 20,000 shares authorized; 0 shares issued and outstanding	—	—
Common stock, $.01 par value; 100,000 shares authorized; 42,004 and 41,818 shares issued and outstanding, respectively	420	418
Additional paid-in capital	77,757	76,257
Accumulated deficit	(80,236)	(108,007)
Total stockholders' deficit	(2,059)	(31,332)
Total liabilities and stockholders' deficit	$303,024	$270,723

See accompanying notes to the consolidated financial statements

SPORTSMAN’S WAREHOUSE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

Amounts in Thousands, Except Per Share Data

	Fiscal Year Ended		
	January 30, 2016	January 31, 2015	February 1, 2014
Net sales	$729,912	$660,003	$643,163
Cost of goods sold	491,382	444,796	435,933
Gross profit	238,530	215,207	207,230
Selling, general, and administrative expenses	179,218	170,315	147,140
Bankruptcy related expenses	—	—	55
Income from operations	59,312	44,892	60,035
Interest expense	(14,156)	(22,480)	(25,447)
Income before income taxes	45,156	22,412	34,588
Income tax expense	17,385	8,628	12,838
Net income	$27,771	$13,784	$21,750
Earnings per share:			
Basic	$0.66	$0.34	$0.66
Diluted	$0.66	$0.34	$0.66
Weighted average shares outstanding:			
Basic	41,966	39,961	33,170
Diluted	42,334	40,141	33,185

See accompanying notes to the consolidated financial statements

SPORTSMAN'S WAREHOUSE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' DEFICIT

Amounts in Thousands

	Common Stock		Restricted nonvoting common stock		Additional paid-in-capital	Accumulated deficit	Total stockholders' deficit
	Shares	Amount	Shares	Amount	Amount	Amount	Amount
Balance at February 2, 2013	27,265	$ 273	5,964	$ 60	$ —	$ (42,177)	$ (41,844)
Dividends	—	—	—	—	—	(101,065)	(101,065)
Repurchase and retirement of restricted nonvoting common stock	—	—	(287)	(3)	—	(299)	(302)
Stock based compensation	—	—	—	—	365	—	365
Net income	—	—	—	—	—	21,750	21,750
Balance at February 1, 2014	27,265	$ 273	5,677	$ 57	$ 365	$ (121,791)	$ (121,096)
Issuance of common shares	8,683	86	—	—	73,305	—	73,391
Conversion of nonvoting common stock to common stock	5,677	57	(5,677)	(57)	—	—	—
Vesting of restricted stock units	193	2	—	—	(2)	—	-
Payment of withholdings on restricted stock units	—	—	—	—	(991)	—	(991)
Excess tax benefit from restricted stock units	—	—	—	—	287	—	287
Stock based compensation	—	—	—	—	3,293	—	3,293
Net income	—	—	—	—	—	13,784	13,784
Balance at January 31, 2015	41,818	$ 418	—	$ —	$ 76,257	$ (108,007)	$ (31,332)
Vesting of restricted stock units	186	2	—	—	(2)	—	—
Payment of withholdings on restricted stock units	—	—	—	—	(1,041)	—	(1,041)
Excess tax benefit from restricted stock units	—	—	—	—	286	—	286
Stock based compensation	—	—	—	—	2,257	—	2,257
Net income	—	—	—	—	—	27,771	27,771
Balance at January 30, 2016	42,004	$ 420	—	$ —	$ 77,757	$ (80,236)	$ (2,059)

See accompanying notes to the consolidated financial statements

SPORTSMAN'S WAREHOUSE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

Amounts in Thousands

	Fiscal Years Ended		
	January 30, 2016	January 31, 2015	February 1, 2014
Cash flows from operating activities:			
Net income	$27,771	$13,784	$21,750
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation of property and equipment	9,763	7,344	4,749
Amortization of discount on debt and deferred financing fees	817	6,497	6,952
Amortization of definite lived intangible	1,806	1,806	1,528
Net increase in deferred rent	1,161	5,397	432
Gain on asset dispositions	—	—	(112)
Deferred income taxes	3,062	(46)	2,169
Excess tax benefits from stock-based compensation arrangements	(286)	(287)	—
Stock-based compensation	2,257	3,293	365
Change in operating assets and liabilities:			
Accounts receivable, net	(44)	(12)	1,052
Merchandise inventories	(31,885)	(24,575)	(28,344)
Prepaid expenses and other	(5,435)	86	(1,522)
Other long-term assets	239	(107)	49
Accounts payable	18,198	836	1,333
Accrued expenses	983	8,127	2,049
Income taxes receivable and payable	7,255	(1,670)	(12,416)
Net cash provided by operating activities	35,662	20,473	34
Cash flows from investing activities:			
Purchase of property and equipment	(33,957)	(30,167)	(20,416)
Purchase of business	—	—	(47,767)
Proceeds from sale-leaseback transactions	19,006	—	—
Proceeds from sale of fixed assets	—	—	124
Net cash used in investing activities	(14,951)	(30,167)	(68,059)
Cash flows from financing activities:			
Net borrowings on line of credit	(16,636)	12,847	29,052
Borrowings on term loan	—	160,000	235,000
Issuance of common stock, net	—	73,393	(302)
Dividends paid	—	—	(101,065)
(Decrease) increase in book overdraft	(1,123)	2,609	5,696
Excess tax benefits from stock-based compensation arrangements	286	287	—
Payment of withholdings on restricted stock units	(1,041)	(993)	—
Payment of deferred financing costs	(239)	(2,227)	(3,960)
Principal payments on unsecured note payable	—	—	(2,756)
Principal payments on long-term debt	(1,600)	(234,225)	(125,863)
Discount on term loan	—	(1,600)	(2,938)
Net cash (used in) provided by financing activities	(20,353)	10,091	32,864

Net change in cash and cash equivalents	358	397	(35,161)
Cash and cash equivalents at beginning of year	1,751	1,354	36,515
Cash and cash equivalents at end of year	$2,109	$1,751	$1,354
Net cash paid during the year for:			
Interest	$12,799	$16,408	$18,979
Income taxes	7,032	10,328	23,089

See accompanying notes to the consolidated financial statements

SPORTSMAN'S WAREHOUSE HOLDINGS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

Amounts in Thousands

(1) Nature of Business

Description of Business

Sportsman's Warehouse Holdings, Inc. ("Holdings"), a Delaware Corporation, and subsidiaries (collectively, the "Company") operate retail sporting goods stores. As of January 30, 2016, the Company operated 64 stores in 19 states.

Voluntary Reorganization under Chapter 11

On March 21, 2009, the Company and all of its subsidiaries filed a voluntary bankruptcy petition for reorganization under Chapter 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the District of Delaware (the "Bankruptcy Court"). On July 30, 2009, the Bankruptcy Court entered an order approving and confirming the Plan of Reorganization (the "Reorganization Plan"). On May 22, 2013, the Company's bankruptcy case was closed after a final decree was entered by the bankruptcy court.

Bankruptcy-Related Expenses

The adoption of fresh start reporting upon emergence from bankruptcy required the Company to allocate the reorganization value to its assets and liabilities in a manner similar to that which is required under Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 805, Business Combinations, including estimated costs required to restructure and emerge from Chapter 11 bankruptcy. The Company incurred certain costs related to restructuring and emergence from Chapter 11 bankruptcy and included a liability as part of the reorganization value at August 14, 2009, the date of emergence from bankruptcy. Amounts greater than the estimated restructuring costs are expensed as incurred and included as a separate component of the consolidated statements of income to arrive at income from operations.

(2) Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements of the Company have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") and include the accounts of its four wholly owned subsidiaries, Sportsman's Warehouse, Inc. ("Sportsman's Warehouse"), Pacific Flyway Wholesale, LLC ("Pacific Flyway"), Sportsman's Warehouse Southwest, Inc., and Minnesota Merchandising Corporation. All intercompany transactions and accounts have been eliminated in consolidation.

Fiscal Year

The Company operates using a 52/53 week fiscal year ending on the Saturday closest to January 31. Fiscal years 2015, 2014 and 2013 ended on January 30, 2016, January 31, 2015 and February 1, 2014, respectively. Fiscal years 2013, 2014, and 2015 contain 52 weeks of operations.

Seasonality

The Company's business is generally seasonal, with a significant portion of total sales occurring during the third and fourth quarters of the fiscal year.

Use of Estimates in the Preparation of Consolidated Financial Statements

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Segment Reporting

The Company operates solely as a sporting goods retailer whose Chief Operating Decision Maker (“CODM”) is the Chief Executive Officer. The CODM reviews financial information presented on a consolidated and individual store and cost center basis, for purposes of allocating resources and evaluating financial performance. The Company’s stores typically have similar square footage and offer essentially the same general product mix. The Company’s core customer demographic remains similar chainwide, as does the Company’s process for the procurement and marketing of its product mix. Furthermore, the Company distributes its product mix chainwide from a single distribution center. Given that the stores have the same economic characteristics, the individual stores are aggregated into one single operating and reportable segment.

Cash and Cash Equivalents

The Company considers cash on hand in stores and highly liquid investments with an initial maturity of three months or less as cash and cash equivalents. Checks issued pending bank clearance that result in overdraft balances for accounting purposes are classified as accrued expenses in the accompanying consolidated balance sheets.

In accordance with the terms of a financing agreement (Note 9), the Company maintains depository accounts with two banks in a lock-box arrangement. Deposits into these accounts are used to reduce the outstanding balance on the line of credit as soon as the respective bank allows the funds to be transferred to the financing company. At January 30, 2016 and January 31, 2015, the combined balance in these accounts were $5,939 and $5,987, respectively. Accordingly, these amounts have been classified as a reduction in the line of credit as if the transfers had occurred on January 30, 2016 and January 31, 2015, respectively.

Accounts Receivable

The Company offers credit terms on the sale of products to certain government and corporate retail customers and requires no collateral from these customers. The Company performs ongoing credit evaluations of its customers’ financial condition and maintains an allowance for doubtful accounts receivable based upon historical experience and a specific review of accounts receivable at the end of each period. Actual bad debts may differ from these estimates and the difference could be significant. At January 30, 2016 and January 31, 2015, the allowance for doubtful accounts receivable totaled $0 and $113, respectively. The activity in the allowance for doubtful accounts was not significant for the fiscal years ended January 30, 2016, January 31, 2015 and February 1, 2014.

Merchandise Inventories

Merchandise inventories are stated at the lower of cost or market. Cost is determined using the weighted average cost method. The Company estimates a provision for inventory shrinkage based on its historical inventory accuracy rates as determined by periodic cycle counts. The allowance for damaged goods from returns is based upon historical experience. The Company also adjusts inventory for obsolete or slow moving inventory based on inventory productivity reports and by specific identification of slow moving or obsolete inventory. The inventory reserves for shrinkage, damaged, or obsolescence totaled $4,306 and $4,089 at January 30, 2016 and January 31, 2015, respectively.

Property and Equipment

Property and equipment are recorded at cost. Leasehold improvements primarily include the cost of improvements funded by landlord incentives or allowances. Maintenance, repairs, minor renewals, and betterments are expensed as incurred. Major renewals and betterments are capitalized. Upon retirement or disposal of assets, the cost and accumulated depreciation and amortization are eliminated from the respective accounts and the related gains or losses are credited or charged to earnings.

Depreciation and amortization of property and equipment is computed using the straight-line method over the estimated useful lives of the related assets. Leasehold improvements are amortized over the shorter of the useful lives of the improvements or the term of the lease. Furniture, fixtures, and equipment, are depreciated over useful lives ranging from 3 to 10 years.

Impairment of Long-Lived Assets

The Company reviews its long-lived assets with definite lives for impairment whenever events or changes in circumstances may indicate that the carrying value of an asset may not be recoverable. The Company uses an estimate of the future undiscounted net cash flows of the related asset or group of assets over their remaining useful lives in measuring whether the assets are recoverable. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized for the amount by which the carrying amount exceeds the estimated fair value of the asset. Impairment of long-lived assets is assessed at the lowest levels for which there are identifiable cash flows that are independent of other groups of assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value, less the estimated costs to sell. No impairment charge to long-lived assets was recorded during the fiscal years ended January 30, 2016, January 31, 2015 or February 1, 2014.

Prepaid Expenses and Other

Prepaid expenses and other primarily consists of prepaid expenses, vendor rebates receivable, vendor advertising receivables and miscellaneous deposits.

Revenue Recognition

Revenue is recognized for retail sales at the time of the sale in the store. The Company records a reserve for estimated product returns in each reporting period, based on its historical experience. The Company's sales returns reserve was $799 and $716 at January 30, 2016, and January 31, 2015, respectively.

Revenue for gift cards sold is deferred and recognized as the gift cards are redeemed for merchandise. Gift card breakage income is recognized based upon historical redemption patterns and represents the balance of gift cards for which the Company believes the likelihood of redemption by the customer is remote. During the fiscal years ended January 30, 2016, January 31, 2015 and February 1, 2014, the Company recognized $846, $833 and $0 of gift card breakage income, respectively. This income is included in the accompanying consolidated statements of income as a reduction in selling, general, and administrative expenses ("SG&A").

In November of 2013, the Company launched a customer loyalty program. Under this program, the Company issues credits in the form of points to loyalty program members. The value of points earned by loyalty program members is included in accrued liabilities and recorded as a reduction of net sales at the time the points are earned. Loyalty breakage income is recognized based upon the balance of loyalty points that have expired after a dormancy period of 18 months. During the fiscal year ended January 30, 2016, the Company recognized $232 of loyalty breakage income. The Company did not recognize any loyalty breakage income for the fiscal year ended January 31, 2015. This income is included in the accompanying consolidated statements of income as an increase in net sales.

Customer deposits on items placed in layaway are recorded as a liability. Revenue is recognized on layaway transactions at the point where the customer takes possession of the merchandise. These liabilities are recorded as unearned revenue in accrued expenses in the consolidated balance sheets.

Sales taxes collected from customers and remitted to governmental authorities are accounted for on a net basis and, therefore, are excluded from net sales in the consolidated statements of income.

Cost of Goods Sold

Cost of goods sold primarily consists of merchandise acquisition costs, including freight-in costs, shipping costs, terms discounts received from the vendor and vendor allowances and rebates associated directly with merchandise. Vendor allowances include allowances and rebates received from vendors. The Company records an estimate of earned allowances based on purchase volumes. These funds are determined for each fiscal year, and the majority is based on various quantitative contract terms. Amounts expected to be received from vendors relating to purchase of merchandise inventories are recognized as a reduction of cost of goods sold as the merchandise is sold. Historical program results and current purchase volumes are reviewed when establishing the estimate for earned allowances.

Shipping and Handling Fees and Costs

All shipping and handling fees billed to customers are recorded as a component of net sales. All costs incurred related to the shipping and handling of products are recorded in cost of sales.

Vendor Allowances

Vendor allowances include price allowances, volume rebates, store opening costs reimbursements, marketing participation and advertising reimbursements received from vendors under the terms of specific arrangements with certain vendors. Vendor allowances related to merchandise are recognized as a reduction of the costs of merchandise as sold. Vendor reimbursements of costs are recorded as a reduction to expense in the period the related cost is incurred based on actual costs incurred. Any cost reimbursements exceeding expenses incurred are recognized as a reduction of the cost of merchandise sold. Volume allowances may be estimated based on historical purchases and estimates of projected purchases.

Tenant Allowances

The Company enters into various types of lease agreements in the operation of its stores, including remodel and build-to-suit arrangements. Under any type of lease agreement, the Company may receive reimbursement from a landlord for some of the costs related to occupancy or tenant improvements per lease provisions. These reimbursements may be referred to as tenant allowances or landlord reimbursements ("tenant allowances"). Reimbursement from a landlord for occupancy or tenant improvements is treated differently depending on the type of arrangement. Under most of the Company’s lease agreements, tenant allowances are included within deferred rent on the accompanying consolidated balance sheets. The deferred rent credit is amortized as rent expense on a straight-line basis over the term of the lease. Landlord reimbursements from these transactions are included in cash flows from operating activities as a change in deferred rent.

In lease agreements where the Company is the deemed owner of the building during the construction period, a deemed sale-leaseback of the building occurs when construction is complete and the lease term begins. Under these lease agreements, as the tenant allowances are received, the value of the Company’s construction-in-progress or leasehold improvements is reduced accordingly. The deemed sale-leaseback transactions are included in cash flows from investing activities.

Health Insurance

The Company maintains for its employees a partially self-funded health insurance plan. The Company maintains stop-loss insurance through an insurance company with a $100 per person deductible and aggregate claims limit above a predetermined threshold. The Company is under contract .

with this insurance company through December 2016. The Company intends to maintain this plan indefinitely. However, the plan may be terminated, modified, suspended, or discontinued at any time for any reason specified by the Company.

The Company has established reserve amounts based upon claims history and estimates of claims that have been incurred but not reported (“IBNR”). As of January 30, 2016 and January 31, 2015, the Company estimated the IBNR to be $980 and $811, respectively. Actual claims may differ from the estimate and such difference could be significant. These reserves are included in accrued expenses in the accompanying consolidated balance sheets.

Workers Compensation Insurance

Effective November 1, 2014, the Company maintains for its employees a high-deductible workers compensation plan. The Company maintains stop-loss insurance through an insurance company with a $150 per claim deductible and aggregate claims limit above a predetermined threshold. The Company intends to maintain this plan indefinitely. However, the plan may be terminated, modified, suspended, or discontinued at any time for any reason specified by the Company. Prior to November 1, 2014, we operated under a guaranteed cost insurance program.

The Company has established reserve amounts based upon claims history and estimates of IBNR. As of January 30, 2016 and January 31, 2015, the Company estimated the IBNR to be $527 and $107, respectively, related to the workers compensation plan. Actual claims may differ from the estimate and such difference could be significant. These reserves are included in accrued expenses in the accompanying consolidated balance sheets.

Operating Leases and Deferred Rent

The Company has various operating lease commitments on its store locations. Certain leases contain rent escalation clauses that require higher rental payments in later years. Leases may also contain rent holidays, or free rents, during the lease term. Rent expense is recognized on a straight-line basis over the lease term. Rent expense in excess of rental payments is recorded as deferred rent on the accompanying consolidated balance sheets.

Advertising

Costs for newspaper, television, radio, and other advertising are expensed in the period in which the advertising occurs. The Company participates in various advertising and marketing cooperative programs with its vendors, who, under these programs, reimburse the Company for certain costs incurred. Payments received under these cooperative programs are recorded as a decrease to expense in the period that the advertising occurred. For the fiscal years ended January 30, 2016, January 31, 2015 and February 1, 2014, net advertising expenses totaled $6,634, $4,629 and $4,685, respectively. These amounts are included in selling, general and administrative expenses in the accompanying consolidated statements of income.

Stock-Based Compensation

Compensation expense is estimated based on grant date fair value on a straight-line basis over the requisite service or offering period. Costs associated with awards are included in compensation expense as a component of selling, general, and administrative expenses.

Income Taxes

The Company recognizes a deferred income tax liability or deferred income tax asset for the future tax consequences attributable to differences between the financial statement basis of existing assets and liabilities and their respective tax basis. Deferred income tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. A valuation allowance is provided against deferred income tax assets when it is more likely than not that all or some portion of the deferred income tax assets will not be realized.

The Company recognizes the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the relevant tax authorities, based on the technical merits of the position. Interest and potential penalties are accrued related to unrecognized tax benefits in the provision for income taxes.

Fair Value of Financial Instruments

The carrying amounts of financial instruments except for long-term debt approximate fair value because of the general short-term nature of these instruments. The carrying amounts of long-term variable rate debt approximate fair value as the terms are consistent with market terms for similar debt instruments. The carrying amount of the Company's financial instruments approximates fair value as of January 30, 2016 and January 31, 2015.

Earnings Per Share

Basic earnings per share is calculated by dividing net income by the weighted-average shares of common stock outstanding, reduced by shares repurchased and held in treasury, during the period. Diluted earnings per share represents basic earnings per share adjusted to include the potentially dilutive effect of outstanding share option awards, nonvested share awards and nonvested share unit awards.

Comprehensive Income

The Company has no components of income that would require classification as other comprehensive income for the fiscal years ended January 30, 2016, January 31, 2015 or February 1, 2014.

Recent Accounting Pronouncements

Revenue from Contracts with Customers

In May 2014, the FASB issued Accounting Standards Update ("ASU") 2014-09 "Revenue from Contracts with Customers" (Topic 606) ("ASU 2014-09"). ASU 2014-09 is a comprehensive new revenue recognition model requiring a company to recognize revenue to depict the transfer of goods or services to a customer at an amount reflecting the consideration it expects to receive in exchange for those goods or services. In August 2015, the FASB issued ASU 2015-14, "Revenue from Contracts with Customers" (Topic 606): Deferral of the Effective Date ("ASU 2015-14). ASU 2015-14 simply formalized a one year deferral of the effective date of ASU 2014-09. As a result of these two standards updates, the Company expects that it will apply the new revenue standard to annual and interim reporting periods beginning after December 15, 2017. In adopting ASU 2014-09 and ASU 2015-14, companies may use either a full retrospective or a modified retrospective approach. Management is evaluating the provisions of ASU 2014-09 and

ASU 2015-14 and has not yet selected a transition method nor have they determined what impact the adoption of ASU 2014-09 and ASU 2015-14 will have on the Company's financial position or results of operations.

Simplifying the Presentation of Debt Issuance Costs

In April 2015, the FASB issued ASU 2015-03, “Simplifying the Presentation of Debt Issuance Costs” (“ASU 2015-03”). ASU 2015-03 requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. ASU 2015-03 is effective for the first interim period for fiscal years beginning after December 15, 2015, with early adoption permitted for financial statements that have not been previously issued. Management does not expect the adoption of ASU 2015-03 to have any effect on the Company’s financial position or results of operations.

Simplifying the Measurement of Inventory

In July 2015, the FASB issued ASU 2015-11, “Simplifying the Measurement of Inventory” (“ASU 2015-11”). Under ASU 2015-11, inventory will be measured at the “lower of cost and net realizable value” and options that currently exist for “market value” will be eliminated. ASU 2015-11 defines net realizable value as the “estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation.” No other changes were made to the current guidance on inventory measurement. ASU 2015-11 is effective for interim and annual periods beginning after December 15, 2016. Early application is permitted and should be applied prospectively. Management is evaluating the provisions of this statement, including which period to adopt, and has not determined what impact the adoption of ASU 2015-11 will have on the Company's financial position or results of operations.

Presentation and Subsequent Measurement of Debt Issuance Costs Association with Line of Credit Arrangements

In August 2015, the FASB issued ASU 2015-15, “Presentation and Subsequent Measurement of Debt Issuance Costs Association with Line of Credit Arrangements” (“ASU 2015-15”). ASU 2015-15 indicates that the guidance in ASU 2015-03 did not address presentation or subsequent measurement of debt issuance costs related to line of credit arrangements. Given the absence of authoritative guidance within ASU 2015-03, the SEC staff has indicated that they would not object to an entity deferring and presenting debt issuance costs ratably over the term of the line of credit arrangement, regardless of whether there are any outstanding borrowings on the line of credit arrangement. Management does not expect the adoption of ASU 2015-15 to have any effect on the Company’s financial position or results of operations.

Simplifying the Presentation of Deferred Taxes

In November 2015, the FASB issued ASU 2015-17 “Balance Sheet Classification of Deferred Taxes” (Topic 740) (“ASU 2015-17”). ASU 2015-17 is intended to simplify the presentation of deferred income taxes and requires that deferred tax liabilities and assets be classified as noncurrent in the company’s consolidated balance sheets. ASU 2015-17 is required to be adopted for annual periods beginning after December 15, 2016, with early adoption permitted. The Company will adopt the provisions of ASU 2015-17 prospectively, with the first annual period of change effective January 31, 2016. Management expects that the adoption of ASU 2015-17 to have an effect on the presentation of the Company’s financial position but no effect on the Company’s results of operations.

Lease Accounting

In February 2016, the FASB issued ASU 2016-02, “Leases” (“ASU 2016-02”). The standard amends the existing accounting standards for lease accounting, including requiring lessees to recognize most leases on their balance sheets and making targeted changes to lessor accounting. ASU 2016-02 will be effective beginning in the first quarter of 2019. Early adoption of ASU 2016-02 is permitted. The new leases standard requires a modified retrospective transition approach for all leases existing at, or entered into after, the date of initial application, with an option to use certain transition relief. Management is currently evaluating the impact of adopting ASU 2016-02 on the Company’s consolidated financial statements.

(3) Supplemental Cash Flow Information

The following table sets forth non-cash investing items for the years ended:

	Fiscal Years Ended		
	January 30, 2016	January 31, 2015	February 1, 2014

Leasehold improvements acquired through tenant allowances	$3,036	$311	$—
Purchases of property and equipment included in accounts payable	1,094	1,263	1,307

(4) Initial Public Offering

On April 23, 2014, the Company completed its initial public offering, pursuant to which it issued and sold 8,333 shares of common stock at a price to the public of $9.50 per share; included in this offering was the sale of 4,167 shares by affiliates of Seidler Equity Partners III, L.P. The total net proceeds raised by the Company were $70,299 after deducting underwriting discounts and commissions of $5,542 and other offering expenses of $3,326. Total net proceeds were used to make an unscheduled early payment on the term loan (Note 10). In connection with the initial public offering, all of the then-outstanding shares of restricted nonvoting common stock automatically converted into shares of common stock.

On May 16, 2014, the underwriters of the Company's initial public offering of common stock partially exercised the over-allotment option granted at the time of the initial public offering to purchase an additional 1,400 shares of common stock at the public offering price of $9.50 per share, less underwriting discounts and commissions, which consists of 350 shares sold by the Company and 1,050 shares sold by affiliates of Seidler Equity Partners III, L.P. The Company received, after deducting underwriting discounts and commissions and estimated offering expenses, approximately $3,100 of net proceeds. Substantially all of the net proceeds were used for the repayment of an additional amount outstanding under the Company's term loans.

(5) Secondary Offering

On September 30, 2015, 6,250 shares of common stock were sold in a secondary offering by certain existing shareholders, including affiliates of Seidler Equity Partners III, L.P. On October 26, 2015, the underwriters of the secondary offering partially exercised the option granted at the time of the secondary offering to purchase an additional 649 shares of common stock at the secondary offering price of $12.25 per share, less underwriting discounts and commissions, which consists solely of shares sold by affiliates of Seidler Equity Partners III, L.P. The Company received no proceeds from the secondary offering or partial exercise of the option. Total expenses incurred related to the secondary offering and the exercise of the option was $727 and is recorded in selling, general, and administrative expenses in the accompanying statements of income.

(6) Property and Equipment

Property and equipment as of January 30, 2016 and January 31, 2015 are as follows:

	January 30, 2016	January 31, 2015
Furniture, fixtures, and equipment	$41,833	$32,678
Leasehold improvements	45,179	34,398
Construction in progress	5,593	7,651
Total property and equipment, gross	92,605	74,727
Less accumulated depreciation and amortization	(30,173)	(20,410)
Total property and equipment, net	$62,432	$54,317

Depreciation expense was $9,763, $7,344 and $4,749 for the fiscal years ended January 30, 2016, January 31, 2015 and February 1, 2014, respectively.

(7) Definite Lived Intangible Asset

Intangible assets increased as a result of the non-compete agreement associated with the acquisition of certain assets and assumed liabilities of Wholesale Sports Outdoor Outfitters (“Wholesale Sports”) in March 2013. The following table summarizes the definite lived intangible assets:

	January 30, 2016			
	Amortization period	Gross carrying amount	Accumulated amortization	Net carrying amount
Amortizing intangible assets:				
Non-compete agreement	5 years	$ 9,063	(5,140)	3,923
Total		$ 9,063	(5,140)	3,923

	January 31, 2015			
	Amortization period	Gross carrying amount	Accumulated amortization	Net carrying amount
Amortizing intangible assets:				
Non-compete agreement	5 years	$ 9,063	(3,334)	5,729
Total		$ 9,063	(3,334)	5,729

Amortization expense for definite lived intangible asset was $1,806 for the fiscal year ended January 30, 2016. Amortization expense for the next three years is $1,806 in fiscal year 2016, $1,806 in fiscal year 2017 and $311 in fiscal year 2018.

(8) Accrued Expenses and Other Liabilities

Accrued expenses and other liabilities consist of the following at January 30, 2016 and January 31, 2015:

	January 30, 2016	January 31, 2015
Book overdraft	$7,182	$8,305
Unearned revenue	14,787	11,663
Accrued payroll and related expenses	8,573	7,104
Sales and use tax payable	2,998	3,708
Litigation accrual	—	4,000
Other	8,940	7,840
	$42,480	$42,620

(9) Revolving Line of Credit

The Company has a senior secured revolving credit facility ("Revolving Line of Credit") with Wells Fargo Bank, National Association ("Wells Fargo") that provides for borrowings in the aggregate amount of up to $135,000, subject to a borrowing base calculation. All borrowings under the revolving credit facility are limited to a borrowing base equal to roughly (1) the lesser of (a) 90% of the net orderly liquidation value of our eligible inventory and (b) 75% of the lower of cost or market value of our eligible inventory, plus (2) 90% of the eligible accounts receivable, less certain reserves against outstanding gift cards, layaway deposits and amounts outstanding under commercial letters of credit, each term as defined in the credit agreement.

Each of the subsidiaries of the Company is a borrower under the revolving credit facility, and all obligations under the revolving credit facility are guaranteed by the Company. All of the Company's obligations under the revolving credit facility are secured by a lien on substantially all of the Company's tangible and intangible assets and the tangible and intangible assets of all of the Company's subsidiaries, including a pledge of all capital stock of each of the Company's subsidiaries. The lien securing the obligations under the revolving credit facility is a first priority lien as to certain liquid assets, including cash, accounts receivable, deposit accounts and inventory. In addition, the credit agreement contains provisions that enable Wells Fargo to require the Company to maintain a lock-box for the collection of all receipts.

As of January 30, 2016 and January 31, 2015, the Company had $31,202 and $47,886, respectively, in outstanding revolving loans under the Revolving Line of Credit. Amounts outstanding are offset on the consolidated balance sheets by amounts in depository accounts under lock-box arrangements, which were $5,939 and $5,987 as of January 30, 2016 and January 31, 2015, respectively. As of January 30, 2016, the Company had stand-by commercial letters of credit of $750 under the terms of the Revolving Line of Credit.

Borrowings under the revolving credit facility bear interest based on either, at the Company's option, the base rate or LIBOR, in each case plus an applicable margin. The base rate is the higher of (1) Wells Fargo's prime rate, (2) the federal funds rate (as defined in the credit agreement) plus 0.50% and (3) the one-month LIBOR (as defined in the credit agreement) plus 1.00%. The applicable margin for loans under the revolving credit facility, which varies based on the average daily availability, ranges from 0.50% to 1.0% per year for base rate loans and from 1.50% to 2.00% per year for LIBOR loans. The weighted average interest rate on the amount outstanding under the revolving credit facility as of January 30, 2016 was 2.16%.

The Company may be required to make mandatory prepayments under the revolving credit facility in the event of a disposition of certain property or assets, in the event of receipt of certain insurance or condemnation proceeds, upon the issuance of certain debt or equity securities, upon the incurrence of certain indebtedness for borrowed money or upon the receipt of certain payments not received in the ordinary course of business.

The Revolving Line of Credit contains customary affirmative and negative covenants, including covenants that limit the Company’s ability to incur, create or assume certain indebtedness, to create, incur or assume certain liens, to make certain investments, to make sales, transfers and dispositions of certain property and to undergo certain fundamental changes, including certain mergers, liquidations and consolidations. The Revolving Line of Credit also requires us to maintain a minimum availability at all times of not less than 10% of the gross borrowing base, and in any event, not less than $5,000. The revolving credit facility also contains customary events of default. The Revolving Line of Credit matures on December 3, 2019.

(10) Long-Term Debt

Long-term debt consisted of the following as of January 30, 2016 and January 31, 2015:

	January 30, 2016	January 31, 2015
Term loan	$158,000	$159,600
Less discount	(1,288)	(1,554)
	156,712	158,046
Less current portion, net of discount	(9,033)	(1,333)
Long-term portion	$147,679	$156,713

Term Loan

The Company has a $160,000 senior secured term loan facility ("Term Loan") with a financial institution. The Term Loan was issued at a price of 99% of the aggregate principal amount and has a maturity date of December 3, 2020.

All of Sportsman's Warehouse, Inc.'s obligations under the Term Loan are guaranteed by Holdings, Minnesota Merchandising Corporation, a wholly owned subsidiary of Holdings, and each of Sportsman's Warehouse, Inc.'s subsidiaries.

The Term Loan is secured by a lien on substantially all of the Company's tangible and intangible assets. The lien securing the obligations under the Term Loan is a first priority lien as to certain non-liquid assets, including equipment, intellectual property, proceeds of assets sales and other personal property.

The Term Loan requires quarterly principal payments of $400 payable on the last business day of each fiscal quarter up to and including October 30, 2020. A final installment payment consisting of the remaining unpaid balance is due on December 3, 2020.

Sportsman's Warehouse, Inc. may be required to make mandatory prepayments on the Term Loan in the event of, among other things, certain asset sales, the receipt of payment in respect of certain insurance claims or the issuance or incurrence of certain indebtedness. Sportsman's Warehouse, Inc. may also be required to make mandatory prepayments based on any excess cash flows as defined in the agreement for the Term Loan. Due to the Company's profitability during fiscal year 2015, the Company is required to make a mandatory prepayment of $7,700 by May 6, 2016, which will reduce the amount outstanding under the term loan.

The Term Loan bears interest at a rate per annum equal to the one-, two-, three-, or six-month LIBOR (or, the nine- or 12-month LIBOR), as defined in the term loan agreement, at the Company's election, which cannot be less than 1.25%, plus an applicable margin of 6.00%.

The Term Loan contain customary affirmative and negative covenants, including covenants that limit the Company's ability to incur, create or assume certain indebtedness, to incur or assume certain liens, to purchase, hold or acquire certain investments, to declare or make certain dividends and distributions and to engage in certain mergers, consolidations and asset sales. The Term Loan also requires the Company to comply with specified financial covenants, including a minimum interest coverage ratio on a trailing twelve month basis and a maximum total net leverage ratio. The Term Loan also contains customary events of default.

As of January 30, 2016, the Term Loan had $156,712 outstanding, net of an unamortized discount of $1,288. During fiscal year 2015, Company recognized $266 of non-cash interest expense with respect to the amortization of this discount. During fiscal year 2014, the Company recognized $2,739 of non-cash interest expense with respect to the amortization of the discount on the prior term loan.

Restricted Net Assets

The provisions of the Term Loan and the Revolving Line of Credit restrict all of the net assets of the Company's consolidated subsidiaries, which constitute all of the net assets on the Company's consolidated balance sheet as of January 30, 2016, from being used to pay any dividends without prior written consent from the financial institutions party to the Company's Term Loan and Revolving Line of Credit.

(11) Sale Leaseback Transactions

During the fiscal year ended January 30, 2016, the Company completed a sale-leaseback of the land and buildings for two store locations. The Company received gross cash proceeds of $12,068, exclusive of transaction costs of approximately $277. The carrying value of the properties sold were $11,964. The Company realized a loss on this transaction of $173, which has been recorded in selling, general, and administrative expenses in the accompanying statements of income. The current and long-term portions of the deferred loss are included in current portion of deferred rent and deferred rent, noncurrent, respectively, in the consolidated balance sheet as of January 20, 2016. Amortization of the deferred loss is reflected as an increase to rent expense and is included within selling, general, and administrative expenses in the consolidated statement of income for the year ended January 30, 2016.

During the fiscal year ended January 30, 2016, the Company completed a deemed sale-leaseback of the land and buildings for three store locations. In each of the related lease agreements for these store locations, the Company was required to pay all construction costs directly with the right of reimbursement up to a pre-determined tenant allowance. Also, the Company indemnified the landlords with respect to costs arising from third-party damage arising from the acts or omission of employees, sub-lessees, assignees, agent, and/or contractors arising during construction. As a result, and, based on appropriate accounting guidance, the Company was deemed the owner of the land and building during the construction period. The deemed sale occurred when the construction of the assets were complete and the lease terms began. At the time of sale, any assets, up to the value of each pre-determined tenant allowance, were written off the Company’s books, and any remaining amounts were considered leasehold improvements. The total value of tenant allowances received during fiscal year 2015 was $5,652.

(12) Common Stock

Holders of common stock are entitled to one vote per share, and to receive dividends and, upon liquidation or dissolution, are entitled to receive all assets available for distribution to stockholders on a proportional basis with the restricted nonvoting common stockholders. The holders have no preemptive or other subscription rights, and there are no redemption or sinking fund provisions with respect to such shares.

(13) Earnings Per Share

Basic earnings per share is calculated by dividing net income by the weighted-average number of shares of common stock outstanding, reduced by the number of shares repurchased and held in treasury, during the period. Diluted earnings per share represents basic earnings per share adjusted to include the potentially dilutive effect of outstanding share option awards, nonvested share awards and nonvested share unit awards.

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

	Fiscal Year Ended		
	January 30, 2016	January 31, 2015	February 1, 2014
Net income	$27,771	$13,784	$21,750

Weighted-average shares of common stock outstanding:			
Basic	41,966	39,961	33,170
Dilutive effect of common stock equivalents	368	180	15
Diluted	42,334	40,141	33,185
Basic earnings per share	$0.66	$0.34	$0.66
Diluted earnings per share	$0.66	$0.34	$0.66

(14) Stock-Based Compensation

Stock-Based Compensation

The Company recognized total stock-based compensation expense of $2,257, $3,293, and $365 during fiscal years 2015, 2014, and 2013, respectively. Compensation expense related to the Company's stock-based payment awards is recognized in selling, general, and administrative expenses in the consolidated statements of income.

Employee Stock Plans

As of January 30, 2016, the number of shares available for awards under the 2013 Performance Incentive Plan (the "2013 Plan") was 1,728,995. As of January 30, 2016, there were 598,697 awards outstanding under the 2013 Plan.

Nonvested Stock Unit Awards

During fiscal year 2015, the Company issued 27,668 nonvested stock units to employees or independent members of the Board of Directors at a weighted average grant date fair value of $11.28 per share. The nonvested stock units issued to employees vest evenly over four years on the grant date anniversary. The nonvested stock units issued to independent members of the Board of Directors vest evenly over 12 months on the grant date anniversary.

During fiscal year 2014, the Company issued 5,000 nonvested stock units to employees at a weighted average grant date fair value of $7.04 per share. The nonvested stock units vest evenly over four years on the grant date anniversary.

As of January 30, 2016 and January 31, 2015, respectively, the Company had $4,279 and $6,268 remaining in unrecognized compensation costs related to nonvested restricted stock units. The weighted average grant date fair value of the outstanding shares were $7.15 and $7.06, respectively. The expected net tax benefit related to the unrecognized compensation costs were $1,647 and $2,413, respectively.

The Company had no net share settlements in fiscal year 2015 or 2014.

The following table sets forth the rollforward of outstanding restricted stock units:

	Shares	Weigthed average grant-date fair value
Balance at January 31, 2015	887,853	$ 7.06
Grants	27,668	11.28
Forfeitures	7,892	7.06
Vested	308,932	7.27
Balance at January 30, 2016	598,697	$ 7.15

	Shares	Weigthed average grant-date fair value
Balance at February 1, 2014	1,193,747	$ 7.06
Grants	5,000	7.04
Forfeitures	13,493	7.06
Vested	297,401	7.06
Balance at January 31, 2015	887,853	$ 7.06

(15) Employee Stock Purchase Plan

In June 2015, the Company’s stockholders approved the Sportsman’s Warehouse Holdings, Inc. Employee Stock Purchase Plan (“ESPP”), which provides for the granting of up to 800 shares of the Company’s common stock to eligible employees. The ESPP period is semi-annual and allows participants to purchase the Company’s stock at 85% of the lower of (i) the market value per share of the common stock on the first day of the offering period or (ii) the market value per share of the common stock on the purchase date. The first plan period began on January 1, 2016. Stock-based compensation expense related to the ESPP in fiscal year 2015 was $15.

The Company uses the Black-Scholes model to estimate the fair value of shares to be issued as of the grant date using the following weighted average assumptions:

	Fiscal Year Ended January 30, 2016	
Risk-free interest rate	0.49	%
Expected life (in years)	0.5	
Expected volatility	36.1	%
Dividend yield	—	

(16) Income Taxes

For the fiscal years ended January 30, 2016, January 31, 2015 and February 1, 2014, the income tax provision consisted of the following:

	January 30, 2016	January 31, 2015	February 1, 2014
Current:			
Federal	$12,341	$7,482	$ 9,421
State	1,982	1,192	1,248
Total current	14,323	8,674	10,669
Deferred:			
Federal	2,746	(103)	1,830
State	316	57	339
Total deferred	3,062	(46)	2,169
Total income tax provision	$17,385	$8,628	$ 12,838

The provision for income taxes differs from the amounts computed by applying the federal statutory rate as follows for the following periods:

	January 30, 2016	January 31, 2015	February 1, 2014
Federal statutory rate	35.0 %	35.0 %	35.0 %
State tax, net of federal benefit	3.5	3.5	3.6
Permanent items	0.2	0.2	0.3
Other items	(0.2)	(0.2)	(1.8)
Effective income tax rate	38.5 %	38.5 %	37.1 %

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at January 30, 2016 and January 31, 2015, respectively, are presented below:

	January 30, 2016	January 31, 2015
Deferred tax assets:		
Accrued liabilities	$468	$444
Allowance for doubtful accounts	—	44
Deferred rent	12,377	11,932
Intangible asset	1,293	—
Inventories	2,335	2,189
Litigation accrual	—	1,540

Net operating loss	—	51
Sales return reserve	308	276
Stock-based compensation	634	600
Total gross deferred tax assets	$17,415	$17,076
Deferred tax liabilities:		
Depreciation	$(11,407)	$(8,125)
Prepaid expenses	(744)	(625)
Total gross deferred tax liabilities	$(12,151)	$(8,750)
Net deferred tax asset	$5,264	$8,326

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As of January 30, 2016 and January 31, 2015, the components of the current and long-term deferred income taxes are as follows:

	January 30, 2016	January 31, 2015
Current deferred tax assets, net:		
Accrued liabilities	$468	$444
Allowance for doubtful accounts	-	44
Inventories	2,335	2,189
Prepaid expenses	(744)	(625)
Sales return reserve	308	276
Stock-based compensation	634	600
Current deferred tax assets, net	$3,001	$2,928
Non-current deferred tax assets, net:		
Deferred rent	$12,377	$11,932
Depreciation	(11,407)	(8,125)
Intangible asset	1,293	—
Litigation accrual	—	1,540
Net operating loss	—	51
Non-current deferred tax assets, net	$2,263	$5,398

Deferred tax assets have resulted primarily from the Company's future deductible temporary differences. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax asset will not be realized. The Company's ability to realize its deferred tax assets depends upon the generation of sufficient future taxable income to allow for the utilization of its deductible temporary differences.

Management evaluates the realizability of the deferred tax assets and the need for additional valuation allowances annually. At January 30, 2016, based on current facts and circumstances, management believes that it is more likely than not that the Company will realize benefit for its gross deferred tax assets.

As of January 30, 2016, the Company had no unrecognized tax benefits. The Company does not anticipate that unrecognized tax benefits will significantly increase or decrease within 12 months of the reporting date. There are no income tax returns that are currently under examination. Federal and state tax years that remain subject to examination are periods ended January 29, 2011 through January 31, 2015.

At January 31, 2015, the Company had state net operating loss carry-forwards of approximately $1,387, which were used to offset taxable income in fiscal year 2015.

The Company's policy is to accrue interest expense, and penalties as appropriate, on estimated unrecognized tax benefits as a charge to interest expense in the consolidated statements of income. During fiscal year 2014, the Company accrued interest and penalties of $14. No interest or penalties were accrued for fiscal year 2015 or fiscal year 2013.

(17) Commitments and Contingencies

Operating Leases

The Company leases its retail store, office space, and warehouse locations under non-cancelable operating leases. Certain of these leases include tenant allowances that are amortized over the life of the lease. In 2015, 2014 and 2013, the Company received tenant allowances of $5,652, $5,129 and $200, respectively. The Company expects to receive $16,705 in tenant allowances under leases during fiscal year 2016. Certain leases require the Company to pay contingent rental amounts based on a percentage of sales, in addition to real estate taxes, insurance, maintenance and other operating expenses associated with the leased premises. These agreements expire at various dates through July 2030 and generally contain three, five-year renewal options. Rent expense under these leases totaled $33,209, $30,520 and $27,118 for the fiscal years ended January 30, 2016, January 31, 2015 and February 1, 2014, respectively.

Future minimum lease payments for non-cancelable operating leases by fiscal year, as of January 30, 2016 are as follows:

Fiscal Year:	
2016	36,840
2017	37,869
2018	37,408
2019	35,076
2020	33,914
Thereafter	114,597
	295,704

Legal Matters

The Company is involved in various legal matters generally incidental to its business. After discussion with legal counsel, the Company believes that the disposition of these matters will not have a material impact on its consolidated financial condition, liquidity, or results of operations.

On March 12, 2014, the Company was added as a defendant to a pending consolidated action filed in the United States District Court, Western District of Washington, captioned as Lacey Market Place Associates II, LLC, et al. v. United Farmers of Alberta Co-Operative Limited, et al., Case No. 2:13-cv-00383-JLR against United Farmers of Alberta Co-Operative Limited (the seller of Wholesale Sports), Wholesale Sports, Alamo Group, LLC and Donald F. Gaube and spouse. The amended complaint was filed by the landlords of two stores that the Company did not assume in the Company’s purchase of assets from Wholesale Sports. Such stores were formerly operated by Wholesale Sports in Skagit and Thurston Counties in Washington. The amended complaint alleged breach of lease, breach of collateral assignment, misrepresentation, intentional interference with contract, piercing the corporate veil and violation of Washington’s Fraudulent Transfer Act. The Company was named as a co-defendant with respect to the intentional interference with contract and fraudulent conveyance claims. The amended complaint sought against the Company and all defendants unspecified money damages, declaratory relief and attorneys’ fees and costs. On January 28, 2015, the court in the Lacey Marketplace action granted in part and denied in part the Company’s motion for summary judgment and dismissed the intentional interference claim against the Company, but declined to dismiss the fraudulent transfer claim.

Trial in the Lacey Marketplace action began March 2, 2015 and concluded March 6, 2015. On March 9, 2015, the jury in the trial awarded $11,887 against the defendants to the action, including the Company. The Company reviewed the decision and accrued $4,000 in its results for the fiscal year ended January 31, 2015 related to this matter. The Company strongly disagreed with the jury’s verdict and filed post-trial motions seeking to have the verdict set aside. On July 30, 2015, the court granted the Company’s motion for judgment as a matter of law. Both United Farmers of Alberta Co-Operative Limited, a co-defendant, and the plaintiff have appealed the court’s summary judgment ruling against the tortious interference claim, and the July 30, 2015 ruling to the appellate court and the appeal is currently in process. Based on the court’s most recent judgment in favor of the Company, the Company determined that the likelihood of loss in this case is not probable, and, as such, the Company reversed the previous accrual of $4,000 in its results for the fiscal year ended January 30, 2016. The reversal of the $4,000 accrual is recorded in selling, general, and administrative expenses in the accompanying statements of income.

(18) Related-Party Transactions

On August 14, 2009, the Company entered into a reimbursement agreement with Seidler Equity Partners III, L.P. Under the terms of this agreement, the Company agreed to reimburse Seidler Equity Partners III, L.P. for various out-of-pocket costs and expenses related to the Company up to a maximum of $150 annually. During the fiscal years ended January 30, 2016, January 31, 2015, and February 1, 2014, the Company made payments of $12, $35 and $18, respectively, under this agreement. At January 30, 2016 and January 31, 2015, there were no amounts payable under the terms of this agreement.

(19) Retirement Plan

The Company sponsors a profit sharing plan (the “Plan”) for which Company contributions are based upon wages paid. As approved by the Board of Directors, the Company makes discretionary contributions to the Plan at rates determined by management. The Company made contributions of $282, $276 and $234 for the fiscal years ended January 30, 2016, January 31, 2015, and February 1, 2014, respectively.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

As of the end of the period covered by this report, management, including our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures pursuant to Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Based upon the evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were effective as of January 30, 2016 to ensure that information required to be disclosed in the reports we file or submit under the Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports we file or submit under the Exchange Act is accumulated and communicated to our management, including our chief executive officer and our chief financial officer, as appropriate to allow timely decisions regarding required disclosure.

Management's Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act for us. Internal control over financial reporting is a process to provide reasonable assurance regarding the reliability of our financial reporting for external purposes in accordance with accounting principles generally accepted in the United States of America.

With the participation of our Chief Executive Officer and our Chief Financial Officer, management evaluated the effectiveness of our internal control over financial reporting as of January 30, 2016, based on the criteria established in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that our internal control over financial reporting was effective as of January 30, 2016.

Exemption from Attestation Report of Independent Registered Public Accounting Firm

This 10-K does not include an attestation report from our registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by our registered public accounting firm pursuant to rules of the SEC that permit emerging growth companies, which we are, to provide only management's report in this 10-K.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting during the 13 weeks ended January 30, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The Company has adopted a Code of Conduct and Ethics applicable to our employees, directors, and officers. This Code of Conduct and Ethics is applicable to our principal executive officer, principal financial officer, principal accounting officer and controller, or persons performing similar functions. The code is available on the Company's website at investors.sportsmanswarehouse.com. To the extent required by rules adopted by the SEC and NASDAQ, we intend to promptly disclose future amendments to certain provisions of the code, or waivers of such provisions granted to executive officers and directors on our website at investors.sportsmanswarehouse.com.

The remaining information required by this Item 10 will be included in our Proxy Statement and is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this Item 11 will be included in our Proxy Statement and is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT RELATED STOCKHOLDER MATTERS

The information required by this Item 12 will be included in our Proxy Statement and is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information required by this Item 13 will be included in our Proxy Statement and is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by this Item 14 will be included in our Proxy Statement and is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) The following documents are filed as part of this report:
1. Financial Statements:
- Report of Independent Registered Public Accounting Firm
- Consolidated Balance Sheets – January 30, 2016 and January 31, 2015
- Consolidated Statements of Income – Years ended January 30, 2016, January 31, 2015 and February 1, 2014
- Consolidated Statements of Stockholders' Deficit – Years ended January 30, 2016, January 31, 2015 and February 1, 2014
- Consolidated Statements of Cash Flows – Years ended January 30, 2016, January 31, 2015 and February 1, 2014
- Notes to Consolidated Financial Statements
2. Exhibits: See Item 15(b) below.

(b) Exhibits

Exhibit Number	Description
3.1	Amended and Restated Certificate of Incorporation of Sportsman's Warehouse Holdings, Inc. (incorporated by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q filed on June 11, 2014).
3.2	Amended and Restated Bylaws of Sportsman's Warehouse Holdings, Inc. (incorporated by reference to Exhibit 3.2 to the Company's Quarterly Report on Form 10-Q filed on June 11, 2014).
4.1	Form of Specimen Common Stock of Sportsman's Warehouse Holdings, Inc. (incorporated by reference to Exhibit 4.1 to Amendment No. 1 to the Company's Registration Statement on Form S-1 (Registration No. 333.1944421) filed on March 24, 2014).
4.2	Registration Rights Agreement, dated April 15, 2014, among Sportsman's Warehouse Holdings, Inc., SEP SWH Holdings, L.P. and New SEP SWH Holdings, L.P. (incorporated by reference to Exhibit 4.2 to the Company's Registration Statement on Form S-1 (Registration No. 333-1944421) filed on March 7, 2014).
10.3.1†	Second Amendment to Credit Agreement (amended and restated Credit Agreement to reflect first amendment), dated as of November 13, 2012, among Sportsman's Warehouse, Inc., as Lead Borrower, the other Borrowers party thereto, Sportsman's Warehouse Holdings, Inc., as a Guarantor, the Lenders party thereto, and Wells Fargo Bank, National Association, as Administrative Agent, Collateral Agent, and Swing Line Lender (incorporated by reference to Exhibit 10.3.2 to the Company's Registration Statement on Form S-1 (Registration No. 333-1944421) filed on March 7, 2014).
10.3.2†	Third Amendment to Credit Agreement, dated as of August 20, 2013, among Sportsman's Warehouse, Inc., as Lead Borrower, the other Borrowers party thereto, Sportsman's Warehouse Holdings, Inc., as a Guarantor, the Lenders party thereto, and Wells Fargo Bank, National Association, as Administrative Agent, Collateral Agent, and Swing Line Lender (incorporated by reference to Exhibit 10.3.4 to the Company's Registration Statement on Form S-1 (Registration No. 333-1944421) filed on March 7, 2014).
10.3.3	Side Letter, dated as of July 8, 2013, from Wells Fargo Bank, National Association to Sportsman's Warehouse, Inc. (incorporated by reference to Exhibit 10.3.3 to the Company's Registration Statement on

	Form S-1 (Registration No. 333-1944421) filed on March 7, 2014).
10.3.4	Side Letter, dated as of October 21, 2013, from Wells Fargo Bank, National Association to Sportsman's Warehouse, Inc. (incorporated by reference to Exhibit 10.3.5 to the Company's Registration Statement on Form S-1 (Registration No. 333-1944421) filed on March 7, 2014).

Exhibit Number	Description
10.3.5	Fourth Amendment to Credit Agreement, dated as of March 20, 2014, among Sportsman's Warehouse, Inc., as Lead Borrower, the other Borrowers party thereto, Sportsman's Warehouse Holdings, Inc., as a Guarantor, the Lenders party thereto, and Wells Fargo Bank, National Association, as Administrative Agent, Collateral Agent, and Swing Line Lender (incorporated by reference to Exhibit 10.3.6 to Amendment No. 1 to the Company's Registration Statement on Form S-1 (Registration No. 333-1944421) filed on March 24, 2014).
10.3.6†	Fifth Amendment to Credit Agreement and Third Amendment to Security Agreement, effective as of December 3, 2014, by and among Wells Fargo Retail Finance, LLC, a global investment company, as Lender, and Sportsman's Warehouse, Inc., as Borrower (incorporated by reference to Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q filed on December 5, 2014).
10.4	Guaranty, dated as of May 28, 2010, by Sportsman's Warehouse Holdings, Inc., as Guarantor, in favor of Wells Fargo Retail Finance, LLC, as Administrative Agent and Collateral Agent, and the Credit Parties (incorporated by reference to Exhibit 10.4 to the Company's Registration Statement on Form S-1 (Registration No. 333-1944421) filed on March 7, 2014).
10.5	Security Agreement, dated as of May 28, 2010, by Sportsman's Warehouse, Inc., Minnesota Merchandising Corp., Sportsman's Warehouse Southwest, Inc. and Pacific Flyway, LLC, as Borrowers, and Sportsman's Warehouse Holdings, Inc., as Guarantor, in favor of Wells Fargo Retail Finance, LLC, as Collateral Agent (incorporated by reference to Exhibit 10.5 to the Company's Registration Statement on Form S-1 (Registration No. 333-1944421) filed on March 7, 2014).
10.6	Form of Agreement between holders of restricted nonvoting common stock and Sportsman's Warehouse Holdings, Inc. (incorporated by reference to Exhibit 10.6 to the Company's Registration Statement on Form S-1 (Registration No. 333-1944421) filed on March 7, 2014).
10.7*	Sportsman's Warehouse Holdings, Inc. 2013 Performance Incentive Plan. (incorporated by reference to Exhibit 10.7 to the Company's Registration Statement on Form S-1 (Registration No. 333-1944421) filed on March 7, 2014).
10.8*	Form of Restricted Stock Unit Award Agreement (incorporated by reference to Exhibit 10.8 to the Company's Registration Statement on Form S-1 (Registration No. 333-1944421) filed on March 7, 2014).
10.9*	Form of Indemnification Agreement for Directors and Executive Officers (incorporated by reference to Exhibit 10.9 to the Company's Registration Statement on Form S-1 (Registration No. 333-1944421) filed on March 7, 2014).
10.10*	Employment Agreement, dated December 10, 2013, between Sportsman's Warehouse Holdings, Inc. and John V. Schaefer (incorporated by reference to Exhibit 10.10 to the Company's Registration Statement on Form S-1 (Registration No. 333-1944421) filed on March 7, 2014).
10.11*	Employment Agreement, dated January 21, 2014, between Sportsman's Warehouse Holdings, Inc. and Kevan P. Talbot (incorporated by reference to Exhibit 10.11 to the Company's Registration Statement on Form S-1 (Registration No. 333-1944421) filed on March 7, 2014).

10.12†	Term Loan Agreement, effective as of December 3, 2014, by and among Cortland Capital Market Services LLC, a global investment company, as Lender, and Sportsman’s Warehouse, Inc., as Borrower (incorporated by reference to Exhibit 10.1 to the Company’s Quarterly Report on Form 10-Q filed on December 5, 2014).
10.13†	Guarantee and Collateral Agreement, effective as of December 3, 2014, by and among Cortland Capital Market Services LLC, a global investment company, as Lender, and Sportsman’s Warehouse, Inc., as Borrower (incorporated by reference to Exhibit 10.2 to the Company’s Quarterly Report on Form 10-Q filed on December 5, 2014).
10.14	Sportsman's Warehouse Holdings, Inc. Employee Stock Purchase Plan (incorporated by reference to Exhibit 10.1 to the Company’s Quarterly Report on Form 10-Q filed on August 28, 2015).

Exhibit Number	Description
10.15	Sixth Amendment to Credit Agreement, effective as of August 26, 2015, by and among Wells Fargo Bank, National Association (as successor by merger to Wells Fargo Retail Finance, LLC), as Lender, and Sportsman's Warehouse, Inc., as Borrower (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q filed on August 28, 2015).
10.16	Seventh Amendment to Credit Agreement, dated as of September 21, 2015, by and among Wells Fargo Bank, National Association, as Administrative Agent, Collateral Agent, and Swing Line Lender, and Sportsman's Warehouse, Inc., as Lead Borrower, and the other parties listed on the signature pages thereto (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the SEC on September 21, 2015).
21.1**	Subsidiaries of Sportsman's Warehouse Holdings, Inc.
23.1**	Consent of KPMG LLP.
23.2**	Consent of Buxton Company.
31.1**	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2**	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1***	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS**	XBRL Instance Document.
101.SCH**	XBRL Taxonomy Extension Schema Document.
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF**	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB**	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase Document.

*	Management contract or compensatory plan or arrangement
**	Filed herewith
***	Furnished herewith
†	Indicates that certain information contained herein has been omitted and confidentially submitted separately with the Securities and Exchange Commission. Confidential treatment has been requested with respect to the omitted portions.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

	SPORTSMAN'S WAREHOUSE HOLDINGS, INC.	
Date: March 24, 2016	By:	/s/ John V. Schaefer John V. Schaefer President and Chief Executive Officer (Principal Executive Officer)
Date: March 24, 2016	By:	/s/ Kevan P. Talbot Kevan P. Talbot Chief Financial Officer and Secretary (Principal Financial and Accounting Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated:

Signature	Title	Date
/s/ John V. Schaefer John V. Schaefer	President, Chief Executive Officer and Director (Principal Executive Officer)	March 24, 2016
/s/ Kevan P. Talbot Kevan P. Talbot	Chief Financial Officer and Secretary (Principal Financial and Accounting Officer)	March 24, 2016
/s/ Christopher Eastland Christopher Eastland	Director	March 24, 2016
/s/ Leonard Lee Leonard Lee	Director	March 24, 2016
/s/ Kent V. Graham Kent V. Graham	Director	March 24, 2016
/s/ Gregory P. Hickey Gregory P. Hickey	Director	March 24, 2016
/s/ Joseph P. Schneider Joseph P. Schneider	Director	March 24, 2016
/s/ Kay L. Toolson Kay L. Toolson	Director	March 24, 2016

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152,091

—

152,091

—

2024 Notes

188,061

—

188,061

—

2021 Asset-Backed Notes

49,199

—

49,199

—

2022 Convertible Notes

236,470

—

236,470

—

Total

$

823,859

$

—

$

625,821

$

198,038

(1) As of March 31, 2018, and December 31, 2017, there were no borrowings outstanding on both the Wells Facility and Union Facility.

4. Borrowings

Outstanding Borrowings

At March 31, 2018 and December 31, 2017, the Company had the following available and outstanding borrowings:

	March 31, 2018			December 31, 2017		
(in thousands)	Total Available	Principal	Carrying Value (1)	Total Available	Principal	Carrying Value (1)
SBA Debentures (2)	$190,200	$190,200	$188,299	$190,200	$190,200	$188,141
2022 Notes	150,000	150,000	147,698	150,000	150,000	147,572
2024 Notes	183,510	183,510	179,161	183,510	183,510	179,001
2021 Asset-Backed Notes	33,575	33,575	33,156	49,153	49,153	48,650
2022 Convertible Notes	230,000	230,000	223,878	230,000	230,000	223,488
Wells Facility (3)	120,000	—	—	120,000	—	—
Union Bank Facility (3)	75,000	—	—	75,000	—	—
Total	$982,285	$787,285	$772,192	$997,863	$802,863	$786,852

(1) Except for the Wells Facility and Union Bank Facility, all carrying values represent the principal amount outstanding less the remaining unamortized debt issuance costs and unaccreted premium or discount, if any, associated with the loan as of the balance sheet date.
(2) At both March 31, 2018 and December 31, 2017, the total available borrowings under the SBA debentures were $190.2 million, of which $41.2 million was available in HT II and $149.0 million was available in HT III.
(3) Availability subject to the Company meeting the borrowing base requirements.

Debt issuance costs are fees and other direct incremental costs incurred by the Company in obtaining debt financing and are recognized as prepaid expenses and amortized over the life of the related debt instrument using the effective yield method or the straight line method, which closely approximates the effective yield method. In accordance with ASC Subtopic 835-30 ("Interest – Imputation of Interest"), debt issuance costs are presented as a reduction to the associated liability balance on the Consolidated Statement of Assets and Liabilities, except for debt issuance costs associated with line-of-credit arrangements. Debt issuance costs, net of accumulated amortization, were as follows as of March 31, 2018 and December 31, 2017:

(in thousands)	March 31, 2018	December 31, 2017
SBA Debentures	$1,901	$ 2,059
2022 Notes	1,548	1,633
2024 Notes	4,417	4,591
2021 Asset-Backed Notes	420	503
2022 Convertible Notes	3,492	3,715
Wells Facility (1)	726	227

Union Bank Facility [(1)]	306	379
Total	$12,810	$ 13,107

(1) As the Wells Facility and Union Bank Facility are line-of-credit arrangements, the debt issuance costs associated with these instruments are presented separately as an asset on the Consolidated Statement of Assets and Liabilities in accordance with ASC Subtopic 835-30.

Long-Term SBA Debentures

On September 27, 2006, HT II received a license to operate as a SBIC under the SBIC program and is able to borrow funds from the SBA against eligible investments and additional contributions to regulatory capital. Under the Small Business Investment Company Act and current SBA policy applicable to SBICs, a SBIC can have outstanding at any time SBA guaranteed debentures up to twice the amount of its regulatory capital. With the Company’s net investment of $44.0 million in HT II as of March 31, 2018, HT II has the capacity to issue a total of $41.2 million of SBA guaranteed debentures, subject to SBA approval, of which $41.2 million was outstanding as of March 31, 2018. As of March 31, 2018, HT II has paid the SBA commitment fees and facility fees of approximately $1.5 million and $3.6 million, respectively. As of March 31, 2018 the Company held investments in HT II in 34 companies with a fair value of approximately $84.9 million, accounting for approximately 5.7% of the Company’s total investment portfolio at March 31, 2018. HT II held approximately $113.1 million in assets and accounted for approximately 5.7% of the Company’s total assets prior to consolidation at March 31, 2018.

On May 26, 2010, HT III received a license to operate as a SBIC under the SBIC program and is able to borrow funds from the SBA against eligible investments and additional contributions to regulatory capital. With the Company’s net investment of $74.5 million in HT III as of March 31, 2018, HT III has the capacity to issue a total of $149.0 million of SBA guaranteed debentures, subject to SBA approval, of which $149.0 million was outstanding as of March 31, 2018. As of March 31, 2018, HT III has paid the SBA commitment fees and facility fees of approximately $1.5 million and $3.6 million, respectively. As of March 31, 2018, the Company held investments in HT III in 47 companies with a fair value of approximately $236.0 million, accounting for approximately 15.9% of the Company’s total investment portfolio at March 31, 2018. HT III held approximately $285.8 million in assets and accounted for approximately 14.4% of the Company’s total assets prior to consolidation at March 31, 2018.

SBICs are designed to stimulate the flow of private equity capital to eligible small businesses. Under present SBA regulations, eligible small businesses include businesses that have a tangible net worth not exceeding $19.5 million and have average annual fully taxed net income not exceeding $6.5 million for the two most recent fiscal years. In addition, SBICs must devote 25.0% of its investment activity to “smaller” enterprises as defined by the SBA. A smaller enterprise is one that has a tangible net worth not exceeding $6.0 million and has average annual fully taxed net income not exceeding $2.0 million for the two most recent fiscal years. SBA regulations also provide alternative size standard criteria to determine eligibility, which depend on the industry in which the business is engaged and are based on such factors as the number of employees and gross sales. According to SBA regulations, SBICs may make long-term loans to small businesses, invest in the equity securities of such businesses and provide them with consulting and advisory services. Through the Company’s wholly owned subsidiaries HT II and HT III, the Company plans to provide long-term loans to qualifying small businesses, and in connection therewith, make equity investments.

HT II and HT III are periodically examined and audited by the SBA’s staff to determine their compliance with SBA regulations. If HT II or HT III fails to comply with applicable SBA regulations, the SBA could, depending on the severity of the violation, limit or prohibit HT II’s or HT III’s use of debentures, declare outstanding debentures immediately due and payable, and/or limit HT II or HT III from making new investments. In addition, HT II or HT III may also be limited in their ability to make distributions to the Company if they do not have sufficient capital in accordance with SBA regulations. Such actions by the SBA would, in turn, negatively affect the Company because HT II and HT III are the Company’s wholly owned subsidiaries. HT II and HT III were in compliance with the terms of the SBIC’s leverage as of March 31, 2018 as a result of having sufficient capital as defined under the SBA regulations.

The rates of borrowings under various draws from the SBA beginning in March 2009 are set semiannually in March and September and range from 2.25% to 4.62% excluding annual fees. Interest payments on SBA debentures are payable semiannually. There are no principal payments required on these issues prior to maturity and no prepayment penalties. Debentures under the SBA generally mature ten years after being borrowed. Based on the initial draw down date of March 2009, the initial maturity of SBA debentures will occur in March 2019. In addition, the SBA charges a fee that is set annually, depending on the Federal fiscal year the leverage commitment was delegated by the SBA, regardless of the date that the leverage was drawn by the SBIC. The annual fees related to HT II debentures that pooled on September 22, 2010 were 0.406% and 0.285%, depending upon the year in which the underlying commitment was closed. The annual fees on other debentures have been set at 0.906%. The annual fees related to HT III debentures that pooled on March 27, 2013 were 0.804%. The annual fees on other debentures have been set at 0.515%. The rates of borrowings on the Company’s SBA debentures range from 3.05% to 5.53% when including these annual fees.

The average amount of debentures outstanding for the three months ended March 31, 2018 for HT II was approximately $41.2 million with an average interest rate of approximately 4.56%. The average amount of debentures outstanding for the three months ended March 31, 2018 for HT III was approximately $149.0 million with an average interest rate of approximately 3.46%.

For the three months ended March 31, 2018 and 2017, the components of interest expense and related fees and cash paid for interest expense for the SBA debentures are as follows:

(in thousands)	Three Months Ended March 31, 2018	2017
Interest expense	$1,718	$1,719
Amortization of debt issuance cost (loan fees)	158	168
Total interest expense and fees	$1,876	$1,887
Cash paid for interest expense	$3,442	$3,442

In aggregate, at March 31, 2018, with the Company’s net investment of $118.5 million, HT II and HT III have the capacity to issue a total of $190.2 million of SBA-guaranteed debentures, subject to SBA approval. At March 31, 2018, the Company has issued $190.2 million in SBA-guaranteed debentures in the Company’s SBIC subsidiaries.

The Company reported the following SBA debentures outstanding principal balances as of March 31, 2018 and December 31, 2017:

(in thousands)

Issuance/Pooling Date	Maturity Date	Interest Rate [1]	March 31, 2018	December 31, 2017
March 25, 2009	March 1, 2019	5.53%	$18,400	$18,400
September 23, 2009	September 1, 2019	4.64%	3,400	3,400
September 22, 2010	September 1, 2020	3.62%	6,500	6,500
September 22, 2010	September 1, 2020	3.50%	22,900	22,900
March 29, 2011	March 1, 2021	4.37%	28,750	28,750
September 21, 2011	September 1, 2021	3.16%	25,000	25,000
March 21, 2012	March 1, 2022	3.28%	25,000	25,000
March 21, 2012	March 1, 2022	3.05%	11,250	11,250
September 19, 2012	September 1, 2022	3.05%	24,250	24,250
March 27, 2013	March 1, 2023	3.16%	24,750	24,750
Total SBA Debentures			$190,200	$190,200

(1) Interest rate includes annual charge

2019 Notes

In April and July 2012, the Company issued $84.5 million in aggregate principal amount of 7.00% notes due 2019 (the "April 2019 Notes"). In September and October 2012, the Company issued $85.9 million in aggregate principal amount of 7.00% notes due 2019 (the "September 2019 Notes"). The April 2019 Notes and September 2019 Notes are together referred to as the "2019 Notes."

In April 2015, the Company redeemed $20.0 million of the $84.5 million issued and outstanding aggregate principal amount of April 2019 Notes, as previously approved by the Board of Directors. In December 2015, the Company redeemed $40.0 million of the $85.9 million issued and outstanding aggregate principal amount of September 2019 Notes, as previously approved by the Board of Directors. The remaining 2019 Notes were fully redeemed on February 24, 2017.

For the three months ended March 31, 2018 and 2017, the components of interest expense and related fees and cash paid for interest expense for the 2019 Notes are as follows:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Interest expense	$—	$1,159
Amortization of debt issuance cost (loan fees)	—	1,546
Total interest expense and fees	$—	$2,705
Cash paid for interest expense	$—	$1,911

2022 Notes

On October 23, 2017, the Company issued $150.0 million in aggregate principal amount of 4.625% Notes due 2022 (the "2022 Notes"). The 2022 Notes were issued pursuant to the Fourth Supplemental Indenture to the Base Indenture, dated October 23, 2017 (the “2022 Notes Indenture”), between the Company and U.S. Bank, National Association, as trustee (the “2022 Trustee”). The sale of the 2022 Notes generated net proceeds of approximately $147.5 million, including a public offering discount of $826,500. Aggregate estimated offering expenses in connection with the transaction, including the underwriter’s discounts and commissions of approximately $975,000, were approximately $1.7 million.

The 2022 Notes mature on October 23, 2022, unless previously repurchased in accordance with their terms. The 2022 Notes bear interest at a rate of 4.625% per year payable semiannually in arrears on April 23 and October 23 of each year, commencing on April 23, 2018.

The 2022 Notes are unsecured obligations of the Company that rank senior in right of payment to all of the Company’s existing and future indebtedness that is expressly subordinated, or junior, in right of payment to the 2022 Notes. The 2022 Notes are not guaranteed by any of the Company’s current or future subsidiaries. The 2022 Notes rank pari passu, or equally, in right of payment with all of the Company’s existing and future liabilities that are not so subordinated, or junior. The 2022 Notes effectively rank subordinated, or junior, to any of the Company’s secured indebtedness (including unsecured indebtedness that the Company later secures) to the extent of the value of the assets securing such indebtedness. The 2022 Notes rank structurally subordinated, or junior, to all existing and future indebtedness (including trade payables) incurred by subsidiaries, financing vehicles or similar facilities of the Company.

The Company may redeem some or all of the 2022 Notes at any time, or from time to time, at the redemption price set forth under the terms of the indenture after September 23, 2022. No sinking fund is provided for the 2022 Notes. The 2022 Notes were issued in denominations of $2,000 and integral multiples of $1,000 thereof. As of March 31, 2018, the Company was in compliance with the terms of the 2022 Notes Indenture.

As of March 31, 2018 and December 31, 2017, the components of the carrying value of the 2022 Notes were as follows:

(in thousands)	March 31, 2018	December 31, 2017
Principal amount of debt	$150,000	$150,000
Unamortized debt issuance cost	(1,548)	(1,633)
Original issue discount, net of accretion	(754)	(795)
Carrying value of 2022 Notes	$147,698	$147,572

For the three months ended March 31, 2018 and 2017, the components of interest expense and related fees and cash paid for interest expense for the 2022 Notes are as follows:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Interest expense	$1,734	$ —
Amortization of debt issuance cost (loan fees)	84	—
Accretion of original issue discount	41	—
Total interest expense and fees	$1,859	$ —
Cash paid for interest expense	$—	$ —

2024 Notes

On July 14, 2014, the Company and U.S. Bank, N.A. (the “2024 Trustee”), entered into the Third Supplemental Indenture (the “Third Supplemental Indenture”) to the Base Indenture between the Company and the 2024 Trustee, dated July 14, 2014, relating to the Company’s issuance, offer and sale of $100.0 million aggregate principal amount of 6.25% unsecured notes due 2024 (the “2024 Notes”). On August 6, 2014, the underwriters issued notification to exercise their over-allotment option for an additional $3.0 million in aggregate principal amount of the 2024 Notes.

On May 2, 2016, the Company closed an underwritten public offering of an additional $72.9 million in aggregate principal amount of the 2024 Notes. The $72.9 million in aggregate principal amount includes $65.4 million from the initial offering on April 21, 2016 and $7.5 million as a result of underwriters exercising a portion of their option to purchase up to an additional $9.8 million in aggregate principal to cover overallotments on April 29, 2016.

On June 27, 2016, the Company closed an underwritten public offering of an additional $60.0 million in aggregate principal amount of the 2024 Notes. On June 30, 2016, the underwriters exercised their option to purchase up to an additional $9.0 million in aggregate principal to cover overallotments, resulting in total aggregate principal of $69.0 million from the offering.

On October 11, 2016, the Company entered into a debt distribution agreement, pursuant to which it may offer for sale, from time to time, up to $150.0 million in aggregate principal amount of 2024 Notes through FBR Capital Markets & Co. acting as its sales agent (the “2024 Notes Agent”). Sales of the 2024 Notes may be made in negotiated transactions or transactions that are deemed to be “at the market offerings” as defined in Rule 415 under the Securities Act of 1933, as amended (the “Securities Act”), including sales made directly on the NYSE, or similar securities exchange or sales made through a market maker other than on an exchange at prices related to prevailing market prices or at negotiated prices.

On October 24, 2017, the Board of Directors approved a redemption of $75.0 million of outstanding aggregate principal amount of the 2024 Notes, which were redeemed on November 23, 2017.

The 2024 Notes Agent receives a commission from the Company equal to up to 2.00% of the gross sales of any 2024 Notes sold through the 2024 Notes Agent under the debt distribution agreement. The 2024 Notes Agent is not required to sell any specific principal amount of 2024 Notes, but will use its commercially reasonable efforts consistent with its sales and trading practices to sell the 2024 Notes. The 2024 Notes are expected to trade “flat,” which means that purchasers in the secondary market will not pay, and sellers will not receive, any accrued and unpaid interest on the 2024 Notes that is not reflected in the trading price.

During the three months ended March 31, 2018, the Company did not sell any notes under the debt distribution agreement. During the year ended December 31, 2017, the Company sold 225,457 notes for approximately $5.6 million in aggregate principal amount. As of March 31, 2018 approximately $136.4 million in aggregate principal amount remains available for issuance and sale under the debt distribution agreement.

All issuances of 2024 Notes rank equally in right of payment and form a single series of notes.

The 2024 Notes will mature on July 30, 2024 and may be redeemed in whole or in part at the Company’s option at any time or from time to time on or after July 30, 2017, upon not less than 30 days nor more than 60 days written notice by mail prior to the date fixed for redemption thereof, at a redemption price of 100% of the outstanding principal amount thereof plus accrued and unpaid interest payments otherwise payable for the then-current quarterly interest period accrued to but not including the date fixed for redemption. The 2024 Notes bear interest at a rate of 6.25% per year payable quarterly on January 30, April 30, July 30 and October 30 of each year, commencing on July 30, 2014, and trade on the NYSE under the trading symbol “HTGX.”

On February 9, 2018, the Company’s Board of Directors approved a redemption of $100.0 million of outstanding aggregate principal amount of the 2024 Notes and notice for such redemption was provided. The Company redeemed this portion of the 2024 Notes on April 2, 2018. See “Note 12 – Subsequent Events.”

The 2024 Notes are the Company’s direct unsecured obligations and rank: (i) pari passu with the Company’s other outstanding and future senior unsecured indebtedness; (ii) senior to any of the Company’s future indebtedness that expressly provides it is subordinated to the 2024 Notes; (iii) effectively subordinated to all the Company’s existing and future secured indebtedness (including indebtedness that is initially unsecured to which the Company subsequently grants security), to the extent of the value of the assets securing such indebtedness; (iv) structurally subordinated to all existing and future indebtedness and other obligations of any of the Company’s subsidiaries.

The Base Indenture, as supplemented by the Third Supplemental Indenture, contains certain covenants including covenants requiring the Company to comply with (regardless of whether it is subject to) the asset coverage requirements set forth in Section 18 (a)(1)(A) of the 1940 Act as modified by Section 61(a)(1) of the 1940 Act and to comply with the restrictions on dividends and other distributions as well as the purchase of capital stock set forth in Section 18(a)(1)(B) of the 1940 Act as modified by Section 61(a)(1) of the 1940 Act. These covenants are subject to important limitations and exceptions that are described in the Base Indenture, as supplemented by the Third Supplemental Indenture. The Base Indenture, as supplemented by the Third Supplemental Indenture, also contains certain reporting requirements, including a requirement that the Company provide financial information to the holders of the 2024 Notes and the 2024 Trustee if the Company should no longer be subject to the reporting requirements under the Exchange Act of 1934, as amended (the “Exchange Act”). The Base Indenture provides for customary events of default and further provides that the 2024 Trustee or the holders of 25% in aggregate principal amount of the outstanding 2024 Notes in a series may declare such 2024 Notes immediately due and payable upon the occurrence of any event of default after expiration of any applicable grace period. As of March 31, 2018, the Company was in compliance with the terms of the Base Indenture as supplemented by the Third Supplemental Indenture.

As of March 31, 2018 and December 31, 2017, the components of the carrying value of the 2024 Notes were as follows:

(in thousands)	March 31, 2018	December 31, 2017
Principal amount of debt	$183,510	$183,510

Unamortized debt issuance cost	(4,417)	(4,591)
Original issue premium, net of amortization	68	82
Carrying value of 2024 Notes	$179,161	$179,001

For the three months ended March 31, 2018 and 2017, the components of interest expense and related fees and cash paid for interest expense for the 2024 Notes are as follows:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Interest expense	$2,881	$3,987
Amortization of debt issuance cost (loan fees)	174	249
Amortization of original issue premium	(13)	(16)
Total interest expense and fees	$3,042	$4,220
Cash paid for interest expense	$2,867	$3,977

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2021 Asset-Backed Notes

On November 13, 2014, the Company completed a $237.4 million term debt securitization in connection with which an affiliate of the Company made an offer of $129.3 million in aggregate principal amount of fixed rate asset-backed notes (the “2021 Asset-Backed Notes”), which were rated A(sf) by Kroll Bond Rating Agency, Inc. The 2021 Asset-Backed Notes were sold by Hercules Capital Funding Trust 2014-1 pursuant to a note purchase agreement, dated as of November 13, 2014, by and among the Company, Hercules Capital Funding 2014-1, LLC as trust depositor (the “2014 Trust Depositor”), Hercules Capital Funding Trust 2014-1 as issuer (the “2014 Securitization Issuer”), and Guggenheim Securities, LLC, as initial purchaser, and are backed by a pool of senior loans made to certain of the Company’s portfolio companies and secured by certain assets of those portfolio companies and are to be serviced by the Company. The securitization has an 18-month reinvestment period during which time principal collections may be reinvested into additional eligible loans. Interest on the 2021 Asset-Backed Notes is paid, to the extent of funds available, at a fixed rate of 3.524% per annum. The 2021 Asset-Backed Notes have a stated maturity of April 16, 2021.

As part of this transaction, the Company entered into a sale and contribution agreement with the 2014 Trust Depositor under which the Company has agreed to sell or have contributed to the 2014 Trust Depositor certain senior loans made to certain of the Company’s portfolio companies (the “2014 Loans”). The Company has made customary representations, warranties and covenants in the sale and contribution agreement with respect to the 2014 Loans as of the date of their transfer to the 2014 Trust Depositor.

In connection with the issuance and sale of the 2021 Asset-Backed Notes, the Company has made customary representations, warranties and covenants in the note purchase agreement. The 2021 Asset-Backed Notes are secured obligations of the 2014 Securitization Issuer and are non-recourse to the Company. The 2014 Securitization Issuer also entered into an indenture governing the 2021 Asset-Backed Notes, which includes customary representations, warranties and covenants. The 2021 Asset-Backed Notes were sold without being registered under the Securities Act (A) in the United States to “qualified institutional buyers” as defined in Rule 144A under the Securities Act and to institutional “accredited investors” (as defined in Rules 501(a)(1), (2), (3) or (7) under the Securities Act) who in each case, are “qualified purchasers” as defined in Section 2(a)(51)(A) of the 1940 Act and pursuant to an exemption under the Securities Act and (B) to non-U.S. purchasers acquiring interest in the 2021 Asset-Backed Notes outside the United States in accordance with Regulation S under the Securities Act. The 2014 Securitization Issuer is not registered under the 1940 Act in reliance on an exemption provided by Section 3(c)(7) thereof and Rule 3a-7 thereunder. In addition, the 2014 Trust Depositor entered into an amended and restated trust agreement in respect of the 2014 Securitization Issuer, which includes customary representation, warranties and covenants.

The 2014 Loans are serviced by the Company pursuant to a sale and servicing agreement, which contains customary representations, warranties and covenants. The Company performs certain servicing and administrative functions with respect to the 2014 Loans. The Company is entitled to receive a monthly fee from the 2014 Securitization Issuer for servicing the 2014 Loans. This servicing fee is equal to the product of one-twelfth (or in the case of the first payment date, a fraction equal to the number of days from and including October 5, 2014 through and including December 5, 2014 over 360) of 2.00% and the aggregate outstanding principal balance of the 2014 Loans plus collections on deposit in the 2014 Securitization Issuer’s collections account, as of the first day of the related collection period (the period from the 5th day of the immediately preceding calendar month through the 4th day of the calendar month in which a payment date occurs, and for the first payment date, the period from and including October 5, 2014, to the close of business on December 5, 2014).The Company also serves as administrator to the 2014 Securitization Issuer under an administration agreement, which includes customary representations, warranties and covenants.

At March 31, 2018 and December 31, 2017, the 2021 Asset-Backed Notes had an outstanding principal balance of $33.6 million and $49.2 million, respectively.

For the three months ended March 31, 2018 and 2017, the components of interest expense and related fees and cash paid for interest expense for the 2021 Asset-Backed Notes are as follows:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Interest expense	$341	$888
Amortization of debt issuance cost (loan fees)	83	210
Total interest expense and fees	$424	$1,098
Cash paid for interest expense	$387	$940

Under the terms of the 2021 Asset-Backed Notes, the Company is required to maintain a reserve cash balance, funded through interest and principal collections from the underlying securitized debt portfolio, which may be used to pay monthly interest and principal payments on the 2021 Asset-Backed Notes. The Company has segregated these funds and classified them as restricted cash. There was approximately $3.6 million and $3.7 million of restricted cash as of March 31, 2018 and December 31, 2017, respectively, funded through interest collections.

Convertible Notes

2022 Convertible Notes

On January 25, 2017, the Company issued $230.0 million in aggregate principal amount of 4.375% Convertible Notes due 2022 (the “2022 Convertible Notes”), which amount includes the additional $30.0 million aggregate principal amount of 2022 Convertible Notes issued pursuant to the initial purchaser’s exercise in full of its overallotment option. The 2022 Convertible Notes were issued pursuant to an Indenture, dated January 25, 2017 (the “2022 Convertible Notes Indenture”), between the Company and U.S. Bank, National Association, as trustee (the “2022 Trustee”). The sale of the 2022 Convertible Notes generated net proceeds of approximately $225.5 million, including $4.5 million of debt issuance costs.

The 2022 Convertible Notes mature on February 1, 2022, unless previously converted or repurchased in accordance with their terms. The 2022 Convertible Notes bear interest at a rate of 4.375% per year payable semiannually in arrears on February 1 and August 1 of each year, commencing on August 1, 2017.

The 2022 Convertible Notes are unsecured obligations of the Company and rank senior in right of payment to the Company’s future indebtedness that is expressly subordinated in right of payment to the 2022 Convertible Notes; equal in right of payment to the Company’s existing and future indebtedness that is not so subordinated; effectively junior in right of payment to any of the Company’s secured indebtedness (including unsecured indebtedness that the Company later secures) to the extent of the value of the assets securing such indebtedness; and structurally junior to all existing and future indebtedness (including trade payables) incurred by the Company’s subsidiaries, financing vehicles or similar facilities.

Prior to the close of business on the business day immediately preceding August 1, 2021, holders may convert their 2022 Convertible Notes only under certain circumstances set forth in the 2022 Convertible Notes Indenture. On or after August 1, 2021 until the close of business on the scheduled trading day immediately preceding the maturity date, holders may convert their 2022 Convertible Notes at any time. Upon conversion, the Company will pay or deliver, as the case may be, at its election, cash, shares of its common stock or a combination of cash and shares of its common stock. The conversion rate is initially 60.9366 shares of common stock per $1,000 principal amount of 2022 Convertible Notes (equivalent to an initial conversion price of approximately $16.41 per share of common stock). The conversion rate will be subject to adjustment in some events but will not be adjusted for any accrued and unpaid interest. In addition, if certain corporate events occur prior to the maturity date, the Company will increase the conversion rate for a holder who elects to convert its 2022 Convertible Notes in connection with such a corporate event in certain circumstances. As of March 31, 2018, the conversion rate was 60.9366 shares of common stock per $1,000 principal amount of Convertible Senior Notes (equivalent to an adjusted conversion price of approximately $16.41 per share of common stock).

The Company may not redeem the 2022 Convertible Notes at its option prior to maturity. No sinking fund is provided for the 2022 Convertible Notes. In addition, if certain corporate events occur, holders of the 2022 Convertible Notes may require the Company to repurchase for cash all or part of their 2022 Convertible Notes at a repurchase price equal to 100% of the principal amount of the 2022 Convertible Notes to be repurchased, plus accrued and unpaid interest through, but excluding, the required repurchase date.

The 2022 Convertible Notes Indenture contains certain covenants, including covenants requiring the Company to comply with Section 18(a)(1)(A) of the 1940 Act as modified by Section 61(a)(1) of the 1940 Act and to provide financial information to the holders of the 2022 Convertible Notes and the 2022 Trustee if the Company ceases to be subject to the reporting requirements of the Exchange Act. These covenants are subject to important limitations and exceptions that are described in the 2022 Convertible Notes Indenture. The Company offered and sold the 2022

Convertible Notes to the initial purchaser in reliance on the exemption from registration provided by Section 4(a)(2) of the Securities Act, for resale by the initial purchaser to qualified institutional buyers (as defined in the Securities Act) pursuant to the exemption from registration provided by Rule 144A under the Securities Act. The Company relied on these exemptions from registration based in part on representations made by the initial purchaser in connection with the sale of the 2022 Convertible Notes.

The 2022 Convertible Notes are accounted for in accordance with ASC Subtopic 470-20 (“Debt Instruments with Conversion and Other Options”). In accounting for the 2022 Convertible Notes, the Company estimated at the time of issuance that the values of the debt and the embedded conversion feature of the 2022 Convertible Notes were approximately 98.5% and 1.5%, respectively. The original issue discount of 1.5%, or $3.4 million, attributable to the conversion feature of the 2022 Convertible Notes was recorded in “capital in excess of par value” in the Consolidated Statement of Assets and Liabilities. As a result, the Company records interest expense comprised of both stated interest expense as well as accretion of the original issue discount resulting in an estimated effective interest rate of approximately 4.76%.

As of March 31, 2018 and December 31, 2017, the components of the carrying value of the 2022 Convertible Notes were as follows:

(in thousands)	March 31, 2018	December 31, 2017
Principal amount of debt	$230,000	$230,000
Unamortized debt issuance cost	(3,492)	(3,715)
Original issue discount, net of accretion	(2,630)	(2,797)
Carrying value of 2022 Convertible Notes	$223,878	$223,488

For the three months ended March 31, 2018 and 2017, the components of interest expense, fees and cash paid for interest expense for the 2022 Convertible notes were as follows:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Interest expense	$2,516	$1,758
Amortization of debt issuance cost (loan fees)	223	133
Accretion of original issue discount	168	112
Total interest expense and fees	$2,907	$2,003
Cash paid for interest expense	$5,031	$—

As of March 31, 2018, the Company is in compliance with the terms of the indentures governing the 2022 Convertible Notes.

Credit Facilities

As of March 31, 2018, and December 31, 2017, the Company has two available credit facilities, the Wells Facility and the Union Bank Facility.

Wells Facility

On June 29, 2015, the Company, through a special purpose wholly owned subsidiary, Hercules Funding II LLC (“Hercules Funding II”), entered into an Amended and Restated Loan and Security Agreement (the “Wells Facility”) with Wells Fargo Capital Finance, LLC, as a lender and as the arranger and the administrative agent, and the lenders party thereto from time to time.

The Wells Facility matures on August 2, 2019, unless terminated sooner in accordance with its terms.

Under the Wells Facility, Wells Fargo Capital Finance, LLC made commitments of $75.0 million, Alostar Bank of Commerce made commitments of $20.0 million, and Everbank Commercial Finance Inc. made commitments of $25.0 million. The Wells Facility contains an accordion feature, in which the Company can increase the credit line up to an aggregate of $300.0 million, funded by additional lenders and with the agreement of Wells Fargo and subject to other customary conditions. The Company expects to continue discussions with various other potential lenders to join the facility; however, there can be no assurances that additional lenders will join the Wells Facility. Borrowings under the Wells Facility generally bear interest at a rate per annum equal to LIBOR plus 3.25%, and the Wells Facility has an advance rate of 50% against eligible debt investments. The Wells Facility is secured by all of the assets of Hercules Funding II. The Wells Facility requires payment of a non-use fee on a scale of 0.0% to 0.50% depending on the average monthly outstanding balance under the facility relative to the maximum amount of commitments at such time. For the three months ended March 31, 2018 and 2017, this non-use fee was $150,000 and $145,000, respectively.

The Wells Facility also includes various financial and other covenants applicable to the Company and the Company's subsidiaries, in addition to those applicable to Hercules Funding II, including covenants relating to certain changes of control of the Company and Hercules Funding II. Among other things, these covenants also require the Company to maintain certain financial ratios, including a maximum debt to worth ratio, minimum interest coverage ratio, minimum portfolio funding liquidity, and a minimum tangible net worth in an amount, when added to outstanding subordinated indebtedness, that is in excess of $500.0 million plus 90% of the cumulative amount of equity raised after June 30, 2014.

As of March 31, 2018, the minimum tangible net worth covenant increased to $742.7 million as a result of the public offering of 18.2 million shares of common stock issued for a total gross proceeds of approximately $242.8 million under an At-The-Market ("ATM") equity distribution agreement (the "Prior Equity Distribution Agreement") with JMP Securities ("JMP") through February 2017, and a new ATM equity distribution agreement in September 2017 (the "Equity Distribution Agreement") with JMP for the issuance of 1.6 million shares for gross proceeds of $20.5 million during 2017, and the issuance of 478,000 shares for gross proceeds of $6.3 million during the three months ended March 31, 2018. See "Note 6 – Stockholder's Equity."

The Wells Facility provides for customary events of default, including, without limitation, with respect to payment defaults, breach of representations and covenants, certain key person provisions, cross acceleration provisions to certain other debt, lien and judgment limitations, and bankruptcy.

On June 20, 2011, the Company paid $1.1 million in structuring fees in connection with the original Wells Facility. In connection with an amendment to the original Wells Facility in August 2014, the Company paid an additional $750,000 in structuring fees and in connection with the amendment in December 2015, the Company paid an additional $188,000 in structuring fees. These fees are being amortized through the end of the term of the Wells Facility.

The Company did not make any draws or repayments on the available facility during the three months ended March 31, 2018. The Company had aggregate draws of $8.5 million on the available facility during the three months ended March 31, 2017 offset by repayments of $13.5 million. There were no borrowings outstanding on the facility as of March 31, 2018 and December 31, 2017.

For the three months ended March 31, 2018 and 2017, the components of interest expense and related fees and cash paid for interest expense for the Wells Facility are as follows:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Interest expense	$—	$2
Amortization of debt issuance cost (loan fees)	44	107
Total interest expense and fees	$44	$109
Cash paid for interest expense	$—	$256

Union Bank Facility

On May 5, 2016, the Company, through a special purpose wholly owned subsidiary, Hercules Funding III LLC (“Hercules Funding III”), as borrower, entered into the credit facility (the “Union Bank Facility”) with MUFG Union Bank, as the arranger and administrative agent, and the lenders party to the Union Bank Facility from time to time. The Union Bank Facility replaced the company’s credit facility (the “Prior Union Bank Facility”) entered into on August 14, 2014 (as amended and restated from time to time) with MUFG Union Bank, as the arranger and administrative agent, and the lenders party to the Prior Union Bank Facility from time to time. Any references to amounts related to the Union Bank Facility prior to May 5, 2016 were incurred and relate to the Prior Union Bank Facility.

On July 18, 2016, the Company entered into the First Amendment to the Loan and Security Agreement, dated as of May 5, 2016 with MUFG Union Bank, N.A. The Amendment amends certain definitions relating to borrowings which accrue interest based on the London Interbank Offered Rate (“LIBOR Loans”) and (ii) the method(s) for calculating interest on and the paying of certain fees related to such LIBOR Loans.

Under the Union Bank Facility, MUFG Union Bank made commitments of $75.0 million. The Union Bank Facility contains an accordion feature, in which the Company can increase the credit line up to an aggregate of $200.0 million, funded by additional lenders and with the agreement of MUFG Union Bank and subject to other customary conditions. There can be no assurances that additional lenders will join the Union Bank Facility to increase available borrowings. Borrowings under the Union Bank Facility generally bear interest at either (i) if such borrowing is a base rate loan, a base rate per annum equal to the federal funds rate plus 1.00%, LIBOR plus 1.00% or MUFG Union Bank’s prime rate, in each case, plus a margin of 1.25% or (ii) if such borrowing is a LIBOR loan, a rate per annum equal to LIBOR plus 3.25%, and the Union Bank Facility generally has an advance rate of 50% against eligible debt investments. The Union Bank Facility is secured by all of the assets of Hercules Funding III.

The Company paid a one-time $562,500 structuring fee in connection with the Union Bank Facility. The Union Bank Facility requires payment of a non-use fee during the revolving credit availability period on a scale of 0.25% to 0.50% depending on the average monthly outstanding balance under the facility relative to the maximum amount of commitments at such time. For the three months ended March 31, 2018, the company incurred non-use fees of $94,000. For the three months ended March 31, 2017, the company incurred non-use fees under the Prior Union Bank Facility of $94,000.

The Union Bank Facility also includes various financial and other covenants applicable to the Company and its subsidiaries, in addition to those applicable to Hercules Funding III, including covenants relating to certain changes of control of the Company and Hercules Funding III. Among other things, these covenants also require the Company to maintain certain financial ratios, including a maximum debt to worth ratio, minimum interest coverage ratio, minimum portfolio funding liquidity, and a minimum tangible net worth in an amount that is in excess of $500.0 million plus 90% of the cumulative amount of equity raised after June 30, 2014.

As of March 31, 2018, the minimum tangible net worth covenant increased to $789.2 million as a result the public offering of 18.2 million shares of common stock issued for a total net proceeds of approximately $239.8 million under the Prior Equity

Distribution Agreement through February 2017, and the issuance of 1.6 million shares for net proceeds of $20.0 million during 2017, and the issuance of 478,000 shares for net proceeds of $6.0 million during the three months ended March 31, 2018 under the Equity Distribution Agreement. See “Note 6 - Stockholder’s Equity.”

The Union Bank Facility provides for customary events of default, including with respect to payment defaults, breach of representations and covenants, servicer defaults, certain key person provisions, cross default provisions to certain other debt, lien and judgment limitations, and bankruptcy.

The Union Bank Facility matures on May 5, 2020, unless terminated sooner in accordance with its terms.

In connection with the Union Bank Facility, the Company and Hercules Funding III also entered into the Sale Agreement, by and among Hercules Funding III, as borrower, the Company, as originator and servicer, and MUFG Union Bank, as agent. Under the Sale Agreement, the Company agrees to (i) sell or transfer certain loans to Hercules Funding III under the MUFG Union Bank Facility and (ii) act as servicer for the loans sold or transferred.

The Company did not make any draws or repayments on the available facility during the three months ended March 31, 2018 and 2017. At March 31, 2018 and December 31, 2017, there were no borrowings outstanding on the Union Bank Facility.

For the three months ended March 31, 2018 and 2017, the components of interest expense and related fees and cash paid for interest expense for the previous and current Union Bank Facility are as follows:

(in thousands)	Three Months Ended March 31, 2018	2017
Interest expense	$—	$—
Amortization of debt issuance cost (loan fees)	74	112
Total interest expense and fees	$74	$112
Cash paid for interest expense	$—	$—

5. Income Taxes

The Company intends to operate so as to qualify to be subject to tax as a RIC under Subchapter M of the Code and, as such, will not be subject to U.S. federal income tax on the portion of taxable income (including gains) distributed as dividends for U.S. federal income tax purposes to stockholders. Taxable income includes the Company’s taxable interest, dividend and fee income, reduced by certain deductions, as well as taxable net realized securities gains. Taxable income generally differs from net income for financial reporting purposes due to temporary and permanent differences in the recognition of income and expenses, and generally excludes net unrealized appreciation or depreciation, as such gains or losses are not included in taxable income until they are realized.

To qualify and be subject to tax as a RIC, the Company is required to meet certain income and asset diversification tests in addition to distributing dividends of an amount generally at least equal to 90% of its investment company taxable income, as defined by the Code and determined without regard to any deduction for distributions paid, to its stockholders. The amount to be paid out as a distribution is determined by the Board of Directors each quarter and is based upon the annual earnings estimated by the management of the Company. To the extent that the Company’s earnings fall below the amount of dividend distributions declared, however, a portion of the total amount of the

Company’s distributions for the fiscal year may be deemed a return of capital for tax purposes to the Company’s stockholders.

During the three months ended March 31, 2018, the Company declared a distribution of $0.31 per share. The determination of the tax attributes of the Company’s distributions is made annually as of the end of the Company’s taxable year generally based upon its taxable income for the full taxable year and distributions paid for the full taxable year. As a result, a determination made on a quarterly basis may not be representative of the actual tax attributes of the Company’s distributions for a full taxable year. If the Company had determined the tax attributes of our distributions taxable year-to-date as of March 31, 2018, 100% would be from our current and accumulated earnings and profits. However, there can be no certainty to stockholders that this determination is representative of what the actual tax attributes of the Company’s 2018 distributions to stockholders will be.

As a RIC, the Company will be subject to a 4% nondeductible U.S. federal excise tax on certain undistributed income unless the Company makes distributions treated as dividends for U.S. federal income tax purposes in a timely manner to its stockholders in respect of each calendar year of an amount at least equal to the sum of (1) 98% of the Company’s ordinary income (taking into account certain deferrals and elections) for each calendar year, (2) 98.2% of the Company’s capital gain net income (adjusted for certain ordinary losses) for the 1-year period ending October 31 of each such calendar year and (3) any ordinary income and capital gain net income realized, but not distributed, in preceding calendar years. The Company will not be subject to this excise tax on any amount on which the Company incurred U.S. federal corporate income tax (such as the tax imposed on a RIC’s retained net capital gains).

Depending on the level of taxable income earned in a taxable year, the Company may choose to carry over taxable income in excess of current taxable year distributions from such taxable income into the next taxable year and incur a 4% excise tax on such taxable income, as required. The maximum amount of excess taxable income that may be carried over for distribution in the next taxable year under the Code is the total amount of distributions paid in the following taxable year, subject to certain declaration and payment guidelines. To the extent the Company chooses to carry over taxable income into the next taxable year, distributions declared and paid by the Company in a taxable year may differ from the Company's taxable income for that taxable year as such distributions may include the distribution of current taxable year taxable income, the distribution of prior taxable year taxable income carried over into and distributed in the current taxable year, or returns of capital.

The Company has taxable subsidiaries which hold certain portfolio investments in an effort to limit potential legal liability and/or comply with source-income type requirements contained in the RIC tax provisions of the Code. These taxable subsidiaries are consolidated for U.S. GAAP and the portfolio investments held by the taxable subsidiaries are included in the Company's consolidated financial statements, and are recorded at fair value. These taxable subsidiaries are not consolidated with the Company for income tax purposes and may generate income tax expense, or benefit, and tax assets and liabilities as a result of their ownership of certain portfolio investments. Any income generated by these taxable subsidiaries generally would be subject to tax at normal corporate tax rates based on its taxable income.

Taxable income for the three months ended March 31, 2018 was approximately $23.6 million or $0.28 per share. Taxable net realized gains for the same period were $219,000 or approximately $0.00 per share. Taxable income for the three months ended March 31, 2017 was approximately $20.5 million or $0.25 per share. Taxable net realized gains for the same period were $3.9 million or approximately $0.05 per share.

For the three months ended March 31, 2018, the Company paid approximately $667,000 of tax expense and had no accrued but unpaid tax expense as of the balance sheet date. For the three months ended March 31, 2017, the Company paid approximately $1.0 million of tax expense and had no accrued but unpaid tax expense as of the balance sheet date.

The Company intends to distribute 100% of spillover earnings from ordinary income from the Company's taxable year ended December 31, 2017 to the Company's stockholders during 2018.

6. Stockholder's Equity

On August 16, 2013, the Company entered into the Prior Equity Distribution Agreement. On March 7, 2016, the Company renewed the Prior Equity Distribution Agreement and on December 21, 2016, we further amended the agreement to increase the total shares available under the program. The Prior Equity Distribution Agreement, as amended, provided that the Company may offer and sell up to 12.0 million shares of its common stock from time to time through JMP, as its sales agent.

On September 7, 2017, the Company terminated the Prior Equity Distribution Agreement and entered into the new Equity Distribution Agreement. As a result, the remaining shares that were available under the Prior Equity Distribution agreement are no longer available for issuance. The Equity Distribution Agreement provides that the Company may offer and sell up to 12.0 million shares of its common stock from time to time through JMP, as its sales agent. Sales of the Company's common stock, if any, may be made in negotiated transactions or transactions that are deemed to be "at the market," as defined in Rule 415 under the Securities Act, including sales made directly on the NYSE or similar securities exchange or sales made to or through a market maker other than on an exchange, at prices related to the prevailing market prices or at negotiated prices.

During the three months ended March 31, 2018, the Company sold 478,000 shares of common stock for total accumulated net proceeds of approximately $6.0 million, including $312,000 of offering expenses under the Equity Distribution Agreement.

During the three months ended March 31, 2017, the Company sold 3.3 million shares of common stock under the Prior Equity Distribution Agreement for total accumulated net proceeds of approximately $46.9 million, including $495,000 of offering expenses.

The Company generally uses net proceeds from these offerings to make investments, to repurchase or pay down liabilities and for general corporate purposes. As of March 31, 2018, approximately 9.9 million shares remain available for issuance and sale under the Equity Distribution Agreement. See “Note 12 – Subsequent Events.”

The Company has issued stock options for common stock subject to future issuance, of which 542,690 and 590,525 were outstanding at March 31, 2018 and December 31, 2017, respectively.

7. Equity Incentive Plan

The Company and its stockholders have authorized and adopted the 2004 Equity Incentive Plan (the "2004 Plan") for purposes of attracting and retaining the services of its executive officers and key employees. Under the 2004 Plan, the Company is authorized to issue 12.0 million shares of common stock.

The Company and its stockholders have authorized and adopted the 2006 Non-Employee Director Plan (the "2006 Plan" and, together with the 2004 Plan, the "Plans") for purposes of attracting and retaining the services of its Board of Directors. On June 21, 2017, the 2006 Plan expired in accordance with its terms and no additional awards may be granted under the 2006 Plan. In the future, we may adopt a Non-Employee Director Plan that, among other things, provides for the issuance of restricted stock to directors. Under the 2006 Plan, the Company is authorized to issue 1.0 million shares of common stock. The Company filed an exemptive relief request with the Securities and Exchange Commission ("SEC") to allow options to be issued under the 2006 Plan which was approved on October 10, 2007.

On June 21, 2007, the stockholders approved amendments to the 2004 Plan and the 2006 Plan allowing for the grant of restricted stock. The amended Plans limit the combined maximum amount of restricted stock that may be issued under both Plans to 10% of the outstanding shares of the Company's stock on the effective date of the Plans plus 10% of the number of shares of stock issued or delivered by the Company during the terms of the Plans. The amendments further specify that no one person shall be granted awards of restricted stock relating to more than 25% of the shares available for issuance under the 2004 Plan. Further, the amount of voting securities that would result from the exercise of all of the Company's outstanding warrants, options and rights, together with any restricted stock issued pursuant to the Plans, at the time of issuance shall not exceed 25% of its outstanding voting securities, except that if the amount of voting securities that would result from such exercise of all of the Company's outstanding warrants, options and rights issued to the Company's directors, officers and employees, together with any restricted stock issued pursuant to the Plans, would exceed 15% of the Company's outstanding voting securities, then the total amount of voting securities that would result from the exercise of all outstanding warrants, options and rights, together with any restricted stock issued pursuant to the Plans, at the time of issuance shall not exceed 20% of the Company's outstanding voting securities.

During 2012, the Compensation Committee adopted a policy that provided for awards with different vesting schedules for short and long-term awards. All restricted stock grants under the 2004 Plan made prior to March 4, 2013 continue to vest on a monthly basis following their one year anniversary over the succeeding 36 months. Under the 2004 Plan, restricted stock awarded subsequent to March 3, 2013 vests subject to continued employment based on two vesting schedules: short-term awards vest one-half on the one year anniversary of the date of the grant and quarterly over the succeeding 12 months, and long-term awards vest one-fourth on the one year anniversary of the date of grant and quarterly over the succeeding 36 months. No restricted stock was granted pursuant to the 2004 Plan prior to 2009.

On December 29, 2016, the Company's Board of Directors approved a further amendment and restatement of the 2004 Plan. The amended plan provides, in addition to the preexisting types of awards available for grant thereunder and among other things, (1) for the grant of restricted stock units; (2) for the deferral of the receipt of the shares of the Company's common stock underlying vested restricted stock units; (3) that grantees may receive up to 10% of the value of the tentative restricted stock unit grants proposed for any grantee in the form of an option to acquire shares of the Company's common stock; (4) that awards of restricted stock units may include performance vesting conditions; (5) that awards may require that all or a portion of the shares of the Company's common stock delivered in respect of any vested restricted stock unit award be subject to a specified post-delivery holding period; and (6) that restricted stock unit awards may accrue distribution equivalents in respect of the Company's common stock underlying any restricted stock unit award payable in the form of cash or additional shares of the Company's common stock to the extent, and in respect of, any vested restricted stock units.

The following table summarizes the common stock option activities for the three months ended March 31, 2018 and 2017:

	Three Months Ended March 31, 2018		2017	
	Common Stock Options	Weighted Average Exercise Price	Common Stock Options	Weighted Average Exercise Price
Outstanding at December 31,	590,525	$ 13.60	668,171	$ 13.73
Granted	22,000	$ 12.11	56,000	$ 14.56
Exercised	(38,208)	$ 11.31	(24,023)	$ 11.23
Forfeited	(20,628)	$ 13.41	(4,723)	$ 10.46
Expired	(10,999)	$ 14.39	—	$ —
Outstanding at March 31,	542,690	$ 13.69	695,425	$ 13.91
Shares Expected to Vest at March 31,	176,076	$ 13.69	297,487	$ 13.91

The following table summarizes common stock options outstanding and exercisable at March 31, 2018:

(Dollars in thousands, except exercise price) Range of exercise prices	Options Outstanding Number of shares	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value	Weighted Average Exercise Price	Options Exercisable Number of shares	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value	Weighted Average Exercise Price
$9.25 - $14.02	305,884	5.67	$ 115,163	$ 12.35	157,004	5.13	$ 87,521	$ 12.07
$14.56 - $16.34	236,806	3.70	—	$ 15.42	209,610	3.40	—	$ 15.49
$9.25 - $16.34	542,690	4.81	$ 115,163	$ 13.69	366,614	4.14	$ 87,521	$ 14.02

Options generally vest 33% one year after the date of grant and ratably over the succeeding 24 months.

All options may be exercised for a period ending seven years after the date of grant. At March 31, 2018 options for 366,614 shares were exercisable at a weighted average exercise price of approximately $14.02 per share with a weighted average remaining contractual term of 4.14 years.

The Company determined that the fair value of options granted under the Plans during the three months ended March 31, 2018 and 2017 was approximately $12,000 and $40,000, respectively. During the three months ended March 31, 2018 and 2017, approximately $14,000 and $20,000 of share-based cost due to stock option grants was expensed, respectively. As of March 31, 2018, there was approximately $85,000 of total unrecognized compensation costs related to stock options. These costs are expected to be recognized over a weighted average remaining vesting period of 1.91 years.

The Company follows ASC Topic 718 (“Compensation – Stock Compensation”) to account for stock options granted. Under ASC Topic 718, compensation expense associated with stock-based compensation is measured at the grant date based on the fair value of the award and is recognized over the vesting period. Determining the appropriate fair value model and calculating the fair value of stock-based awards at the grant date requires judgment, including estimating stock price volatility, forfeiture rate and expected option life. The fair value of options granted is based upon a Black Scholes option pricing model using the assumptions in the following table for the three months ended March 31, 2018 and 2017:

	Three Months Ended March 31, 2018	2017
Expected Volatility	21.19%	23.07%
Expected Dividends	10%	10%
Expected term (in years)	4.5	4.5
Risk-free rate	2.19% - 2.64%	1.70% - 2.02%

During the three months ended March 31, 2018 and 2017, the Company granted 334,995 shares and 4,464 shares, respectively, of restricted stock awards pursuant to the Plans. The Company determined that the fair value of restricted stock awards granted under the Plans during the three months ended March 31, 2018 and 2017 was approximately $4.4 million and $65,000, respectively. As of March 31, 2018, there was approximately $5.7 million of total unrecognized compensation costs related to restricted stock awards. These costs are expected to be recognized over a weighted average remaining vesting period of 2.22 years.

The following table summarizes the activities for the Company’s unvested restricted stock awards for the three months ended March 31, 2018 and 2017:

	Three Months Ended March 31,			
	2018		2017	
	Restricted Stock Awards	Weighted Average Grant Date Fair Value	Restricted Stock Awards	Weighted Average Grant Date Fair Value
Unvested at December 31,	261,245	$ 12.43	799,558	$ 12.54
Granted	334,995	$ 13.04	4,464	$ 14.56
Vested	(83,054)	$ 13.03	(240,299)	$ 12.42
Forfeited	(1,168)	$ 12.01	(1,602)	$ 13.60
Unvested at March 31,	512,018	$ 12.73	562,121	$ 12.61

During the three months ended March 31, 2018, and 2017, the Company granted 411,689 shares and 600,461 shares of restricted stock units pursuant to the Plans based on the December 2016 amended terms. The Company determined that the fair value of restricted stock units granted under the Plans during the three months ended March 31, 2018 and 2017, was approximately $5.4 million and $8.5 million. As of March 31, 2018, there was approximately $9.6 million of total unrecognized compensation costs related to restricted stock units. These costs are expected to be recognized over a weighted average remaining vesting period of 2.32 years.

The following table summarizes the activities for the Company’s unvested restricted stock units for the three months ended March 31, 2018:

	Three Months Ended March 31, 2018		Three Months Ended March 31, 2017	
	Restricted Stock Units	Weighted Average Grant Date Fair Value	Restricted Stock Units	Weighted Average Grant Date Fair Value
Unvested at December 31,	594,322	$ 12.99	—	$ —
Granted	411,689	$ 13.04	600,461	$ 13.94
Distribution Equivalent Unit Granted	20,386	$ 12.42	11,788	$ 13.94
Vested (1)	(198,006)	$ 12.91	—	$ —
Forfeited	(3,544)	$ 12.66	(1,078)	$ 13.92
Unvested at March 31,	824,847	$ 12.69	611,171	$ 13.94

(1) Pursuant to the December 29, 2016 amendment and restatement of the 2004 plan, receipt of the shares of the Company’s common stock underlying vested restricted stock units will be deferred for 4 years from grant date unless certain conditions are met. As such, vested restricted stock units will not be issued as common stock upon vesting until the completion of the deferral period.

During the three months ended March 31, 2018, the Company expensed approximately $2.3 million of compensation expense related to restricted stock awards and restricted stock units. The Company had approximately $1.8 million in compensation expense related to restricted stock awards during the three months ended March 31, 2017.

The SEC, through an exemptive order granted on June 22, 2010, approved amendments to the Plans which allow participants to elect to have the Company withhold shares of the Company’s common stock to pay for the exercise price and applicable taxes with respect to an option exercise (“net issuance exercise”). The exemptive order also permits the holders of restricted stock to elect to have the Company withhold shares of the Company’s stock to pay the applicable taxes due on restricted stock at the time of vesting. Each individual can make a cash payment at the time of option exercise or to pay taxes on restricted stock.

8. Earnings Per Share

Shares used in the computation of the Company’s basic and diluted earnings per share are as follows:

(in thousands, except per share data)	Three Months Ended March 31, 2018	2017
Numerator		
Net increase in net assets resulting from operations	$5,946	$(5,588)
Less: Distributions declared-common and restricted shares	(26,419)	(25,667)

Undistributed earnings	(20,473)	(31,255)
Undistributed earnings-common shares	(20,473)	(31,255)
Add: Distributions declared-common shares	26,247	25,479
Numerator for basic and diluted change in net assets per common share	$5,774	$(5,776)
Denominator		
Basic weighted average common shares outstanding	84,596	81,420
Common shares issuable	70	—
Weighted average common shares outstanding assuming dilution	84,666	81,420
Change in net assets per common share		
Basic	$0.07	$(0.07)
Diluted	$0.07	$(0.07)

In the table above, unvested share-based payment awards that have non-forfeitable rights to distributions or distribution equivalents are treated as participating securities for calculating earnings per share. Unvested common stock options and restricted stock units are also considered for the purpose of calculating diluted earnings per share.

For the three months ended March 31, 2018 and 2017, the effect of the 2022 Convertible Notes under the treasury stock method is anti-dilutive and, accordingly, is excluded from the calculation of diluted earnings per share.

The calculation of change in net assets resulting from operations per common share—assuming dilution, excludes all anti-dilutive shares. For the three months ended March 31, 2018, the number of anti-dilutive shares, as calculated based on the weighted average closing price of the Company's common stock for the periods, consisted of 4.3 million shares related to 2022 Convertible Notes, 73,024 shares of unvested common stock options, and no shares of unvested restricted stock units. For the three months ended March 31, 2017, the number of anti-dilutive shares, as calculated based on the weighted average closing price of the Company's common stock for the periods, consisted of 1.2 million shares related to 2022 Convertible Notes, 72,796 shares of unvested common stock options, and 30,649 shares of unvested restricted stock units.

At March 31, 2018 and December 31, 2017, the Company was authorized to issue 200.0 million shares of common stock with a par value of $0.001. Each share of common stock entitles the holder to one vote.

9. Financial Highlights

Following is a schedule of financial highlights for the three months ended March 31, 2018 and 2017:

	Three Months Ended March 31,	
	2018	2017
Per share data [(1)]:		
Net asset value at beginning of period	$9.96	$9.90
Net investment income	0.31	0.28
Net realized gain (loss) on investments	(0.06)	0.04
Net unrealized appreciation (depreciation) on investments	(0.18)	(0.39)
Total from investment operations	0.07	(0.07)
Net increase (decrease) in net assets from capital share transactions [(1)]	(0.03)	0.22
Distributions of net investment income [(6)]	(0.31)	(0.31)
Distributions of capital gains [(6)]	—	—
Stock-based compensation expense included in investment income [(2)]	0.03	0.02
Net asset value at end of period	$9.72	$9.76
Ratios and supplemental data:		
Per share market value at end of period	$12.10	$15.13
Total return [(3)]	(5.44%)	9.47%
Shares outstanding at end of period	85,239	82,801
Weighted average number of common shares outstanding	84,596	81,420
Net assets at end of period	$828,731	$807,896
Ratio of total expense to average net assets [(4)]	10.64%	11.48%
Ratio of net investment income before investment gains and losses to average net assets [(4)]	12.25%	10.99%
Portfolio turnover rate [(5)]	15.62%	10.89%
Weighted average debt outstanding	$795,060	$785,915
Weighted average debt per common share	$9.40	$9.65

(1) All per share activity is calculated based on the weighted average shares outstanding for the relevant period, except net increase (decrease) in net assets from capital share transactions, which is based on the common shares outstanding as of the relevant balance sheet date.

(2) Stock option expense is a non-cash expense that has no effect on net asset value. Pursuant to ASC Topic 718 (“Compensation – Stock Compensation”), net investment income includes the expense associated with the granting of stock options which is offset by a corresponding increase in paid-in capital.
(3) The total return for the three months ended March 31, 2018 and 2017 equals the change in the ending market value over the beginning of the period price per share plus distributions paid per share during the period, divided by the beginning price assuming the distribution is reinvested on the date of the distribution. As such, the total return is not annualized. The total return does not reflect any sales load that must be paid by investors.
(4) These ratios are calculated based on weighted average net assets for the relevant period and are annualized. The ratio of total expense to average net assets for the period ended March 31, 2017 was incorrectly computed. The ratio was revised from 7.99% as previously disclosed to 11.48% as adjusted. The ratio was incorrectly computed for June 30, 2017 as well. It will be revised from 7.63% as previously disclosed to 11.24% in the June 30, 2018 Consolidated Financial Statements.
(5) The portfolio turnover rate for the three months ended March 31, 2018 and 2017 equals the lesser of investment portfolio purchases or sales during the period, divided by the average investment portfolio value during the period. As such, portfolio turnover rate is not annualized.
(6) Includes distributions on unvested shares.

10. Commitments and Contingencies

The Company's commitments and contingencies consist primarily of unused commitments to extend credit in the form of loans to the Company's portfolio companies. A portion of these unfunded contractual commitments are dependent upon the portfolio company reaching certain milestones before the debt commitment becomes available. Furthermore, the Company's credit agreements contain customary lending provisions which allow the Company relief from funding obligations for previously made commitments in instances where the underlying company experiences materially adverse events that affect the financial condition or business outlook for the Company. Since a portion of these commitments may expire without being drawn, unfunded contractual commitments do not necessarily represent future cash requirements. As such, the Company's disclosure of unfunded contractual commitments includes only those which are available at the request of the portfolio company and unencumbered by milestones.

At March 31, 2018, the Company had approximately $51.9 million of unfunded commitments, including undrawn revolving facilities, which were available at the request of the portfolio company and unencumbered by milestones.

The Company also had approximately $174.0 million of non-binding term sheets outstanding at March 31, 2018. Non-binding outstanding term sheets are subject to completion of the Company's due diligence and final investment committee approval process, as well as the negotiation of definitive documentation with the prospective portfolio companies. These non-binding term sheets generally convert to contractual commitments in approximately 90 days from signing. Not all non-binding term sheets are expected to close and do not necessarily represent future cash requirements.

The fair value of the Company's unfunded commitments is considered to be immaterial as the yield determined at the time of underwriting is expected to be materially consistent with the yield upon funding, given that interest rates are generally pegged to market indices and given the existence of milestones, conditions and/or obligations imbedded in the borrowing agreements.

As of March 31, 2018, the Company's unfunded contractual commitments available at the request of the portfolio company, including undrawn revolving facilities, and unencumbered by milestones are as follows:

(in thousands) Portfolio Company	Unfunded Commitments [1]
Chemocentryx, Inc.	$ 10,000
Evernote Corporation	10,000
Proterra, Inc.	10,000
Impact Radius Holdings, Inc.	5,000
Wrike, Inc.	5,000
Achronix Semiconductor Corporation	5,000
Oak Street Health	5,000
Lithium Technologies, Inc.	878
Greenphire	500
Insurance Technologies Corp.	500
Total	$ 51,878

(1) Amount represents unfunded commitments, including undrawn revolving facilities, which are available at the request of the portfolio company. Amount excludes unfunded commitments which are unavailable due to the borrower having not met certain milestones.

Certain premises are leased or licensed under agreements which expire at various dates through June 2027. Total rent expense amounted to approximately $451,000 and $444,000 during the three months ended March 31, 2018 and 2017.

The Company’s contractual obligations as of March 31, 2018 include:

	Payments due by period (in thousands)				
Contractual Obligations (1)	Total	Less than 1 year	1 - 3 years	3 - 5 years	After 5 years
Borrowings (2)(3)(5)	$787,285	$151,975	$61,550	$490,250	$83,510
Operating Lease Obligations (4)	17,290	2,436	5,005	5,912	3,937
Total	$804,575	$154,411	$66,555	$496,162	$87,447

(1) Excludes commitments to extend credit to the Company’s portfolio companies.
(2) Includes $190.2 million in principal outstanding under the SBA debentures, $150.0 million of the 2022 Notes, $183.5 million of the 2024 Notes, $33.6 million of the 2021 Asset-Backed Notes and $230.0 million of the 2022 Convertible Notes as of March 31, 2018.
(3) Amounts represent future principal repayments and not the carrying value of each liability. See Note 4 to the Company’s consolidated financial statements.
(4) Facility leases and licenses.
(5) Reflects announced redemption of a portion of the 2024 Notes in April 2018. See “Note 4 – Borrowings.”

The Company may, from time to time, be involved in litigation arising out of its operations in the normal course of business or otherwise. Furthermore, third parties may try to seek to impose liability on the Company in connection with the activities of its portfolio companies. While the outcome of any current legal proceedings cannot at this time be predicted with certainty, the Company does not expect any current matters will materially affect the Company’s financial condition or results of operations; however, there can be no assurance whether any pending legal proceedings will have a material adverse effect on the Company’s financial condition or results of operations in any future reporting period.

11. Recent Accounting Pronouncements

In January 2016, the FASB issued Accounting Standards Update (“ASU”) 2016-01, “Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities,” which, among other things, requires that (i) all equity investments, other than equity-method investments, in unconsolidated entities generally be measured at fair value through earnings and (ii) an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. Additionally, the ASU changes the disclosure requirements for financial instruments. ASU 2016-01 is effective for annual reporting periods, and the interim periods within those periods, beginning after December 15, 2017. The Company has adopted this standard, which did not have a material impact, on its consolidated financial statements and related disclosures for the periods presented.

In February 2016, the FASB issued ASU 2016-02, “Leases (Topic 842),” which, among other things, requires recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous U.S. GAAP. Additionally, the ASU requires the classification of all cash payments on leases within operating activities in the Consolidated Statement of Cash Flows. ASU 2016-02 is effective for annual reporting periods, and the interim periods within those periods, beginning after December 15, 2018. Early adoption is permitted. The Company anticipates an increase in the recognition of right-of-use assets and lease liabilities, however, the Company does not believe that ASU 2016-02 will have a material impact on its consolidated financial statements and disclosures.

In August 2016, the FASB issued ASU 2016-15, “Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments,” which addresses eight specific cash flow issues including, among other things, the classification of debt prepayment or debt extinguishment costs. ASU 2016-15 is effective for annual reporting periods, and the interim periods within those periods, beginning after December 15, 2017. The Company has adopted this standard, which did not have a material impact, on its consolidated financial statements and related disclosures for the periods presented.

In October 2016, the SEC adopted new rules and forms and amended other rules to enhance the reporting and disclosure of information by registered investment companies. As part of these changes, the SEC amended Regulation S-X to standardize and enhance disclosures in investment company financial statements. Implementation of the new or amended rules is required for reporting periods ending after August 1, 2017. The Company has reviewed the requirements and adopted the amendments to Regulation S-X on its consolidated financial statements and related disclosures for the periods presented.

In November 2016, the FASB issued ASU 2016-18, “Statement of Cash Flows (Topic 230),” which requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The new guidance is effective for interim and annual periods beginning after December 15, 2017. The Company has adopted this standard, which did not have a material impact, on its consolidated financial statements and related disclosures for the periods presented.

12. Subsequent Events

Distribution Declaration

On April 25, 2018 the Board of Directors declared a cash distribution of $0.31 per share to be paid on May 21, 2018 to stockholders of record as of May 14, 2018. This distribution represents the Company’s fifty-first consecutive distribution since the Company’s IPO, bringing the total cumulative distribution to date to $14.33 per share.

Redemption of 2024 Notes

On February 9, 2018, the Company’s Board of Directors approved a redemption of $100.0 million of outstanding aggregate principal amount of the 2024 Notes, which were redeemed on April 2, 2018.

ATM Equity Program Issuances

Subsequent to March 31, 2018 and as of April 30, 2018, the Company sold 679,800 shares of common stock for total accumulated net proceeds of approximately $8.2 million, including $74,000 of offering expenses, under the Equity Distribution Agreement with JMP. As of April 30, 2018, approximately 9.2 million shares remain available for issuance and sale under the Equity Distribution Agreement.

2025 Notes

On April 26, 2018, the Company issued $75.0 million in aggregate principal amount of 5.25% notes due 2025 (the “2025 Notes”). The 2025 Notes were issued pursuant to the Fifth Supplemental Indenture to the Base Indenture, dated April 26, 2018 (the “2025 Notes Indenture”), between the Company and U.S. Bank, National Association, as trustee. The sale of the 2025 Notes generated net proceeds of approximately $73.0 million. Aggregate estimated offering expenses in connection with the transaction, including the underwriter’s discount and commissions, were approximately $2.0 million.

The 2025 Notes will mature on April 30, 2025, unless previously repurchased in accordance with their terms. The 2025 Notes bear interest at a rate of 5.25% per year payable quarterly in arrears on January 30, April 30, July 30 and October 30 of each year, commencing on July 30, 2018.

The 2025 Notes will be the Company’s direct unsecured obligations and rank pari passu, or equally in right of payment, with all outstanding and future unsecured unsubordinated indebtedness issued by Hercules Capital, Inc.

The Company may redeem some or all of the 2025 Notes at any time, or from time to time, at the redemption price set forth under the terms of the indenture after April 30, 2021. No sinking fund is provided for the 2025 Notes. The 2025 Notes were issued in denominations of $25 and integral multiples of $25 thereof.

The 2025 Notes are listed on the NYSE, and trade on the NYSE under the symbol “HCXZ.”

Portfolio Company Developments

As of April 30, 2018, the Company held warrants or equity positions in three companies that have filed registration statements on Form S-1 with the SEC in contemplation of potential initial public offerings. All three companies filed confidentially under the Jumpstart Our Business Startups Act of 2012, or the JOBS Act. There can be no assurance that companies that have yet to complete their initial public offerings will do so in a timely manner or at all. In addition, subsequent to March 31, 2018, the following companies announced or completed liquidity events:

1. In March 2018, our portfolio company IntegenX, Inc., the market leader of rapid human DNA identification technology for use in forensics and law enforcement applications, announced that they have been acquired by Thermo Fisher Scientific Inc., the world leader in serving science. Terms of the transaction were not disclosed.
2. In April 2018, our portfolio company, DocuSign, Inc. completed its initial public offering.

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

Forward-Looking Statements

The matters discussed in this report, as well as in future oral and written statements by management of Hercules Capital, Inc., that are forward-looking statements are based on current management expectations that involve substantial risks and uncertainties which could cause actual results to differ materially from the results expressed in, or implied by, these forward- looking statements. Forward-looking statements relate to future events or our future financial performance. We generally identify forward-looking statements by terminology such as "may," "will," "should," "expects," "plans," "anticipates," "could," "intends," "target," "projects," "contemplates," "believes," "estimates," "predicts," " "continue" or the negative of these terms or other similar expressions. Important assumptions include our ability to originate new investments, achieve certain margins and levels of profitability, the availability of additional capital, and the ability to maintain certain debt to asset ratios. In light of these and other uncertainties, the inclusion of a projection or forward-looking statement in this report should not be regarded as a representation by us that our plans or objectives will be achieved. The forward-looking statements contained in this report include statements as to:

- our current and future management structure;
- our future operating results;
- our business prospects and the prospects of our prospective portfolio companies;
- the impact of investments that we expect to make;
- our informal relationships with third parties including in the venture capital industry;
- the expected market for venture capital investments and our addressable market;
- the dependence of our future success on the general economy and its impact on the industries in which we invest;
- our ability to access debt markets and equity markets;
- the ability of our portfolio companies to achieve their objectives;
- our expected financings and investments;
- our regulatory structure and tax status;
- our ability to operate as a business development company, a SBIC and a RIC;
- the adequacy of our cash resources and working capital;
- the timing of cash flows, if any, from the operations of our portfolio companies;
- the timing, form and amount of any distributions;
- the impact of fluctuations in interest rates on our business;
- the valuation of any investments in portfolio companies, particularly those having no liquid trading market; and
- our ability to recover unrealized losses.

The following discussion should be read in conjunction with our consolidated financial statements and related notes and other financial information appearing elsewhere in this report. In addition to historical information, the following discussion and other parts of this report contain forward-looking information that involves risks and uncertainties. Our actual results could differ materially from those anticipated by such forward-looking information due to the factors discussed under Item 1A— "Risk Factors" of Part II of this quarterly report on Form 10-Q, Item 1A— "Risk Factors" of our annual report on Form 10-K filed with the Securities and Exchange Commission ("SEC") on February 22, 2018 and under "Forward-Looking Statements" of this Item 2.

Overview

We are a specialty finance company focused on providing senior secured loans to high-growth, innovative venture capital-backed companies in a variety of technology, life sciences, and sustainable and renewable technology industries. We source our investments through our principal office located in Palo Alto, CA, as well as through our additional offices in Boston, MA, New York, NY, Washington, DC, Hartford, CT, and San Diego, CA.

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Our goal is to be the leading structured debt financing provider for venture capital-backed companies in technology-related industries requiring sophisticated and customized financing solutions. Our strategy is to evaluate and invest in a broad range of technology-related industries including technology, drug discovery and development, biotechnology, life sciences, healthcare, and sustainable and renewable technology and to offer a full suite of growth capital products. We invest primarily in structured debt with warrants and, to a lesser extent, in senior debt and equity investments. We invest primarily in private companies but also have investments in public companies.

We use the term “structured debt with warrants” to refer to any debt investment, such as a senior or subordinated secured loan, that is coupled with an equity component, including warrants, options or other rights to purchase common or preferred stock. Our structured debt with warrants investments typically are secured by some or all of the assets of the portfolio company. We also provide “unitranche” loans, which are loans that combine both senior and mezzanine debt, generally in a first lien position.

Our investment objective is to maximize our portfolio total return by generating current income from our debt investments and capital appreciation from our warrant and equity-related investments. Our primary business objectives are to increase our net income, net operating income and NAV by investing in structured debt with warrants and equity of venture capital-backed companies in technology-related industries with attractive current yields and the potential for equity appreciation and realized gains. Our equity ownership in our portfolio companies may exceed 25% of the voting securities of such companies, which represents a controlling interest under the 1940 Act. In some cases, we receive the right to make additional equity investments in our portfolio companies in connection with future equity financing rounds. Capital that we provide directly to venture capital-backed companies in technology-related industries is generally used for growth and general working capital purposes as well as in select cases for acquisitions or recapitalizations.

We also make investments in qualifying small businesses through our two wholly owned small business investment companies (“SBICs”). Our SBIC subsidiaries, Hercules Technology II, L.P. (“HT II”) and Hercules Technology III, L.P. (“HT III”), hold approximately $113.1 million and $285.8 million in assets, respectively, and accounted for approximately 5.7% and 14.4% of our total assets, respectively, prior to consolidation at March 31, 2018. In aggregate, at March 31, 2018, with our net investment of $118.5 million, HT II and HT III have the capacity to issue a total of $190.2 million of SBA-guaranteed debentures, subject to Small Business Administration (“SBA”) approval. At March 31, 2018, we have issued $190.2 million in SBA-guaranteed debentures in our SBIC subsidiaries.

We have qualified as and have elected to be treated for tax purposes as a RIC under Subchapter M of the Code. Pursuant to this election, we generally will not be subject to corporate-level taxes on any income and gains that we distribute as dividends for federal income tax purposes to our stockholders. However, our qualification and election to be treated as a RIC requires that we comply with provisions contained in Subchapter M of the Code. For example, as a RIC we must earn 90% or more of our gross income during each taxable year from qualified sources, typically referred to as “good income,” as well as satisfy certain quarterly asset diversification and annual income distribution requirements.

We are an internally managed, non-diversified, closed-end investment company that has elected to be regulated as a business development company under the 1940 Act. As a business development company, we are required to comply with certain regulatory requirements. For instance, we generally have to invest at least 70% of our total assets in “qualifying assets,” which includes securities of private U.S. companies, cash, cash equivalents and high-quality debt investments that mature in one year or less.

Our portfolio is comprised of, and we anticipate that our portfolio will continue to be comprised of, investments primarily in technology related companies at various stages of their development. Consistent with requirements under the 1940 Act, we invest primarily in United-States based companies and to a lesser extent in foreign companies.

We regularly engage in discussions with third parties with respect to various potential transactions. We may acquire an investment or a portfolio of investments or an entire company or sell a portion of our portfolio on an opportunistic basis. We, our subsidiaries or our affiliates may also agree to manage certain other funds that invest in debt, equity or provide other financing or services to companies in a variety of industries for which we may earn management or other fees for our services. We may also invest in the equity of these funds, along with other third parties, from which we would seek to earn a return and/or future incentive allocations. Some of these transactions could be material to our business. Consummation of any such transaction will be subject to completion of due diligence, finalization of key business and financial terms (including price) and negotiation of final definitive documentation as well as a number of other factors and conditions including, without limitation, the approval of our board of directors and required regulatory or third party consents and, in certain cases, the approval of our stockholders. Accordingly, there can be no assurance that any such transaction would be consummated. Any of these transactions or funds may require significant management resources either during the transaction phase or on an ongoing basis depending on the terms of the transaction.

Portfolio and Investment Activity

The total fair value of our investment portfolio was approximately $1.5 billion at both March 31, 2018 and December 31, 2017. The fair value of our debt investment portfolio at March 31, 2018 was approximately $1.3 billion, compared to a fair value of approximately $1.4 billion December 31, 2017. The fair value of the equity portfolio at March 31, 2018 was approximately $114.0 million, compared to a fair value of approximately $89.4 million at December 31, 2017. The fair value of the warrant portfolio at March 31, 2018 was approximately $33.3 million, compared to a fair value of approximately $36.8 million at December 31, 2017.

Portfolio Activity

Our investments in portfolio companies take a variety of forms, including unfunded contractual commitments and funded investments. From time to time, unfunded contractual commitments depend upon a portfolio company reaching certain milestones before the debt commitment is available to the portfolio company, which is expected to affect our funding levels. These commitments are subject to the same underwriting and ongoing portfolio maintenance as the on-balance sheet financial instruments that we hold. Debt commitments generally fund over the two succeeding quarters from close. Not all debt commitments represent future cash requirements. Similarly, unfunded contractual commitments may expire without being drawn and thus do not represent future cash requirements.

Prior to entering into a contractual commitment, we generally issue a non-binding term sheet to a prospective portfolio company. Non-binding term sheets are subject to completion of our due diligence and final investment committee approval process, as well as the negotiation of definitive documentation with the prospective portfolio companies. These non-binding term sheets generally convert to contractual commitments in approximately 90 days from signing. Not all non-binding term sheets are expected to close and do not necessarily represent future cash requirements.

Our portfolio activity for the three months ended March 31, 2018 and the year ended December 31, 2017 was comprised of the following:

(in millions)	March 31, 2018	December 31, 2017
Debt Commitments [1]		
New portfolio company	$232.6	$ 773.2
Existing portfolio company	5.0	98.8
Total	$237.6	$ 872.0
Funded and Restructured Debt Investments [2]		
New portfolio company	$162.6	$ 578.9
Existing portfolio company	45.0	175.9
Total	$207.6	$ 754.8
Funded Equity Investments		
New portfolio company	$27.4	7.1
Existing portfolio company	1.3	2.9
Total	$28.7	$ 10.0
Unfunded Contractual Commitments [3]		
Total	$51.9	$ 73.6
Non-Binding Term Sheets		
New portfolio company	$146.0	$ 122.0

Existing portfolio company	28.0	—
Total	$174.0	$ 122.0

(1) Includes restructured loans and renewals in addition to new commitments.
(2) Funded amounts include borrowings on revolving facilities.
(3) Amount represents unfunded commitments, including undrawn revolving facilities, which are available at the request of the portfolio company. Amount excludes unfunded commitments which are unavailable due to the borrower having not met certain milestones.

We receive principal payments on our debt investment portfolio based on scheduled amortization of the outstanding balances. In addition, we receive principal repayments for some of our loans prior to their scheduled maturity date. The frequency or volume of these early principal repayments may fluctuate significantly from period to period. During the three months ended March 31, 2018, we received approximately $273.3 million in aggregate principal repayments. Of the approximately $273.3 million of aggregate principal repayments, approximately $29.8 million were scheduled principal payments and approximately $243.5 million were early principal repayments related to 12 portfolio companies. Of the approximately $243.5 million early principal repayments, approximately $18.5 million were early repayments due to merger and acquisition transactions for two portfolio companies.

Total portfolio investment activity (inclusive of unearned income and excluding activity related to taxes payable, and escrow receivables) as of and for the three months ended March 31, 2018 and the year ended December 31, 2017 was as follows:

(in millions)	March 31, 2018	December 31, 2017
Beginning portfolio	$1,542.2	$1,423.9
New fundings and restructures	236.3	764.8
Warrants not related to current period fundings	(0.10)	0.6
Principal payments received on investments	(29.8)	(119.5)
Early payoffs	(243.5)	(505.6)
Accretion of loan discounts and paid-in-kind principal	8.2	36.5
Net acceleration of loan discounts and loan fees due to early payoff or restructure	(5.3)	(8.1)
New loan fees	(2.8)	(9.8)
Sale of investments	—	(11.0)
Loss on investments due to write offs	(6.5)	(39.6)
Net change in unrealized appreciation (depreciation)	(15.1)	10.0
Ending portfolio	$1,483.6	$1,542.2

As of March 31, 2018, we held warrants or equity positions in three companies that have filed registration statements on Form S-1 with the SEC in contemplation of potential initial public offerings. All three companies filed confidentially under the Jumpstart Our Business Startups Act of 2012, or the JOBS Act. There can be no assurance that companies that have yet to complete their initial public offerings will do so in a timely manner or at all.

Changes in Portfolio

We generate revenue in the form of interest income, primarily from our investments in debt securities, and commitment and facility fees. Interest income is recognized in accordance with the contractual terms of the loan agreement to the extent that such amounts are expected to be collected. Fees generated in connection with our debt investments are recognized over the life of the loan or, in some cases, recognized as earned. In addition, we generate revenue in the form of capital gains, if any, on warrants or other equity-related securities that we acquire from our portfolio companies. Our investments generally range from $12.0 million to $40.0 million, although we may make investments in amounts above or below that range. As of March 31, 2018, our debt investments have a term of between two and seven years and typically bear interest at a rate ranging from 5.1% to 14.5%. In addition to the cash yields received on our debt investments, in some instances, our debt investments may also include any of the following: exit fees, balloon payment fees, commitment fees, success fees, payment-in-kind ("PIK") provisions or prepayment fees which may be required to be included in income prior to receipt.

Interest on debt securities is generally payable monthly, with amortization of principal typically occurring over the term of the investment. In addition, our loans may include an interest-only period ranging from three to eighteen months or longer. In limited instances in which we choose to defer amortization of the loan for a period of time from the date of the initial investment, the principal amount of the debt securities and any accrued but unpaid interest become due at the maturity date.

Loan origination and commitment fees received in full at the inception of a loan are deferred and amortized into fee income as an enhancement to the related loan's yield over the contractual life of the loan. We recognize nonrecurring fees amortized over the remaining term of the loan commencing in the quarter relating to specific loan modifications. We had approximately $33.0 million of unamortized fees at March 31, 2018, of which approximately $28.8 million was included as an offset to the cost basis of our current debt investments and approximately $4.2 million was deferred contingent upon the occurrence of a funding or milestone. At December 31, 2017, we had approximately $33.3 million of unamortized fees, of which approximately $29.3 million was included as an offset to the cost basis of our current debt investments and approximately $4.0 million was deferred contingent upon the occurrence of a funding or milestone.

Loan exit fees to be paid at the termination of the loan are accreted into interest income over the contractual life of the loan. At March 31, 2018, we had approximately $22.9 million in exit fees receivable, of which approximately $20.4 million was included as a component of the cost basis of our current debt investments and approximately $2.5 million was a deferred receivable related to expired commitments. At December 31, 2017, we had approximately $27.5 million in exit fees receivable, of which approximately $23.9 million was included as a component of the cost basis of our current debt investments and approximately $3.6 million was a deferred receivable related to expired commitments.

We have debt investments in our portfolio that contain a PIK provision. The PIK interest, computed at the contractual rate specified in each loan agreement, is recorded as interest income and added to the principal balance of the loan on specified capitalization dates. To maintain our ability to be subject to tax as a RIC, this non-cash source of income must be distributed to stockholders with other sources of income in the form of dividend distributions even though we have not yet collected the cash. Amounts necessary to pay these distributions may come from available cash or the liquidation of certain investments. We recorded approximately $2.3 million and $2.2 million in PIK income in the three months ended March 31, 2018 and 2017, respectively.

The core yield on our debt investments, which excludes the effects of fee and income accelerations attributed to early payoffs, restructuring, loan modifications and other one-time events and includes income from expired commitments, was 11.9% and 12.2% during the three months ended March 31, 2018 and 2017, respectively. The effective yield on our debt investments, which includes the effects of fee and income accelerations attributed to early payoffs, restructuring, loan modifications and other one-time events, was 14.3% and 13.4% for the three months ended March 31, 2018 and 2017, respectively. The effective yield is derived by dividing total investment income by the weighted average earning investment portfolio assets outstanding during the quarter, excluding non-interest earning assets such as warrants and equity investments. Both the core yield and effective yield may be higher than what our common stockholders may realize as the core yield and effective yield do not reflect our expenses and any sales load paid by our common stockholders.

The total return for our investors was approximately -5.4% and 9.5% during the three months ended March 31, 2018 and 2017, respectively. The total return equals the change in the ending market value over the beginning of the period price per share plus dividend distributions paid per share during the period, divided by the beginning price assuming the distribution is reinvested on the date of the distribution. The total return does not reflect any sales load that must be paid by investors. See “Note 9 – Financial Highlights” included in the notes to our consolidated financial statements appearing elsewhere in this report.

Portfolio Composition

Our portfolio companies are primarily privately held companies and public companies which are active in the software, drug discovery & development, internet consumer & business services, sustainable and renewable technology, drug delivery, healthcare services, medical devices & equipment, media/content/info, diversified financial services, information services, electronics & computer hardware, consumer & business products, surgical devices, communications & networking, biotechnology tools, semiconductors, diagnostic and specialty pharmaceuticals industry sectors. These sectors are characterized by high margins, high growth rates, consolidation and product and market extension opportunities. Value for companies in these sectors is often vested in intangible assets and intellectual property.

As of March 31, 2018, approximately 78.1% of the fair value of our portfolio was composed of investments in five industries: 26.5% investments in the software industry, 26.1% investments in the drug discovery & development industry, 12.0% investments in the internet consumer & business services industry, 7.8% investments in the sustainable and renewable technology industry, and 5.7% investments in the drug delivery.

Industry and sector concentrations vary as new loans are recorded and loans pay off. Loan revenue, consisting of interest, fees, and recognition of gains on equity and warrants or other equity-related interests, can fluctuate materially when a loan is paid off or a warrant or equity interest is sold. Revenue recognition in any given year can be highly concentrated in several portfolio companies.

For the three months ended March 31, 2018 and the year ended December 31, 2017, our ten largest portfolio companies represented approximately 29.7% and 34.6% of the total fair value of our investments in portfolio companies, respectively. At March 31, 2018 and December 31, 2017, we had five and seven investments, respectively, that represented 5% or more of our net assets. At March 31, 2018, we had seven equity investments representing approximately 64.9% of the total fair value of our equity investments, and each represented 5% or more of the total fair value of our equity investments. At December 31, 2017, we had nine equity investments which represented approximately 67.1% of the total fair value of our equity investments, and each represented 5% or more of the total fair value of our equity investments.

As of March 31, 2018, approximately 96.5% of the debt investment portfolio was priced at floating interest rates or floating interest rates with a Prime or LIBOR-based interest rate floor. As a result, we believe we are well positioned to benefit should market interest rates continue to rise.

As of March 31, 2018, 85.6% of our debt investments were in a senior secured first lien position, 13.4% were secured by a senior second priority security interest in all of the portfolio company’s assets, other than intellectual property, and the remaining 1.0% were unsecured as a result of the terms of the acquisition of two of our portfolio companies. In the majority of cases, we collateralize our investments by obtaining a first priority security interest in a portfolio company’s assets, which may include its intellectual property. In other cases, we may obtain a negative pledge covering a company’s intellectual property.

At March 31, 2018, of the approximately 85.6% of our debt investments in a senior secured first lien position, 48.0% were secured by a first priority security in all of the assets of the portfolio company, including its intellectual property, 33.3% were secured by a first priority security in all of the assets of the portfolio company and the portfolio company was prohibited from pledging or encumbering its intellectual property, or subject to a negative pledge. Another 1.7% of the Company's debt investments were senior secured by the equipment of the portfolio company, and 2.6% were in a first lien "last-out" senior secured position with security interest in all assets of the portfolio company whereby the "last-out" loans will be subordinated to the "first-out" portion of the unitranche loan in a liquidation, sale or other disposition.

Our investments in senior secured debt with warrants have detachable equity enhancement features, typically in the form of warrants or other equity-related securities designed to provide us with an opportunity for capital appreciation. These features are treated as OID and are accreted into interest income over the term of the loan as a yield enhancement. Our warrant coverage generally ranges from 3% to 20% of the principal amount invested in a portfolio company, with a strike price generally equal to the most recent equity financing round. As of March 31, 2018, we held warrants in 134 portfolio companies, with a fair value of approximately $33.3 million. The fair value of our warrant portfolio decreased by approximately $3.5 million, as compared to a fair value of $36.8 million at December 31, 2017 primarily related to the slight decrease in portfolio companies and valuation of the portfolio.

Our existing warrant holdings would require us to invest approximately $84.0 million to exercise such warrants as of March 31, 2018. Warrants may appreciate or depreciate in value depending largely upon the underlying portfolio company's performance and overall market conditions. Of the warrants that we have monetized since inception, we have realized multiples in the range of approximately 1.02x to 29.06x based on the historical rate of return on our investments. However, our warrants may not appreciate in value and, in fact, may decline in value. Accordingly, we may experience losses from our warrant portfolio.

Portfolio Grading

We use an investment grading system, which grades each debt investment on a scale of 1 to 5 to characterize and monitor our expected level of risk on the debt investments in our portfolio with 1 being the highest quality. The following table shows the distribution of our outstanding debt investments on the 1 to 5 investment grading scale at fair value as of March 31, 2018 and December 31, 2017, respectively:

(in thousands)	March 31, 2018			December 31, 2017		
Investment Grading	Number of Companies	Debt Investments at Fair Value	Percentage of Total Portfolio	Number of Companies	Debt Investments at Fair Value	Percentage of Total Portfolio
1	10	$ 141,761	10.6 %	12	$ 345,191	24.4 %
2	36	599,767	44.9 %	32	583,017	41.2 %
3	30	548,038	41.0 %	32	443,775	31.3 %
4	4	33,573	2.5 %	4	41,744	2.9 %
5	5	13,187	1.0 %	5	2,257	0.2 %
	85	$ 1,336,326	100.0 %	85	$ 1,415,984	100.0 %

As of March 31, 2018, our debt investments had a weighted average investment grading of 2.43 on a cost basis, as compared to 2.17 at December 31, 2017. Our policy is to lower the grading on our portfolio companies as they approach the point in time when they will require additional equity capital. Additionally, we may downgrade our portfolio companies if they are not meeting our financing criteria or are underperforming relative to their respective business plans. Various companies in our portfolio will require additional funding in the near term or have not met their business plans and therefore have been downgraded until their funding is complete or their operations improve. The decline in weighted average investment grading at March 31, 2018 from December 31, 2017 is primarily due to the payoff of our credit rating 1 positions, including Machine Zone, Inc. and Alimera Sciences, Inc., as well as the downgrade of Fuze, Inc., Clarabridge and Proterra, Inc., from a credit rating 2 to a credit rating 3. In addition, two positions were downgraded to a credit rating 5, while two positions that were rated 5 as of December 31, 2017 were sold or liquidated during the period.

At March 31, 2018, we had four debt investments on non-accrual with a cumulative investment cost and fair value of approximately \$12.3 million and \$0, respectively. At December 31, 2017, we had five debt investments on non-accrual with cumulative investment cost and fair value of approximately \$14.8 million and \$340,000, respectively. The decrease in the cumulative cost of debt investments on non-accrual between March 31, 2018 and December 31, 2017 is the result of the liquidation of one debt investment that was on non-accrual at December 31, 2017. We recognized a realized loss of approximately \$1.7 million on the write-off of the investment.

Results of Operations

Comparison of the three months ended March 31, 2018 and 2017

Investment Income

Interest Income

Total investment income for the three months ended March 31, 2018 was approximately $48.7 million as compared to approximately $46.4 million for the three months ended March 31, 2017.

Interest income for the three months ended March 31, 2018 totaled approximately $43.0 million as compared to approximately $42.9 million for the three months ended March 31, 2017. The increase in interest income for the three months ended March 31, 2018 as compared to the same period ended March 31, 2017 is primarily attributable to an increase in interest accelerations due to early loan repayments and other one-time events, offset by a decrease in recurring interest income.

Of the $43.0 million in interest income for the three months ended March 31, 2018, approximately $39.3 million represents recurring income from the contractual servicing of our loan portfolio and approximately $3.7 million represents income related to the acceleration of income due to early loan repayments and other one-time events during the period. Income from recurring interest and the acceleration of interest income due to early loan repayments represented $40.0 million and $2.9 million, respectively, of the $42.9 million interest income for the three months ended March 31, 2017.

The following table shows the PIK-related activity for the three months ended March 31, 2018 and 2017, at cost:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Beginning PIK interest receivable balance	$15,487	$9,930
PIK interest income during the period	2,308	2,215
PIK accrued (capitalized) to principal but not recorded as income during the period	—	—
Payments received from PIK loans	(7,983)	(46)
Realized gain (loss)	—	—
Ending PIK interest receivable balance	$9,812	$12,099

The increase in PIK interest income during the three months ended March 31, 2018 as compared to the three months ended March 31, 2017 is due to an increase in the weighted average principal outstanding of loans which bear PIK interest. This increase is partially offset by an increase in the number of PIK loans that paid off during the period.

Fee Income

Fee income from commitment, facility and loan related fees for the three months ended March 31, 2018 totaled approximately $5.7 million as compared to approximately $3.5 million for the three months ended March 31, 2017. The increase in fee income for the three months ended March 31, 2018 is primarily due to an increase in the acceleration of unamortized fees due to early repayments and one-time fees between periods.

Of the $5.7 million in fee income for the three months ended March 31, 2018, approximately $1.3 million represents income from recurring fee amortization and approximately $4.4 million represents income related to the acceleration of unamortized fees due to early repayments, including one-time fees of $3.2 million for the period. Income from recurring fee amortization and the acceleration of unamortized fees due to early loan repayments represented $2.1 million and $1.4 million, respectively, of the $3.5 million in income for the three months ended March 31, 2017.

In certain investment transactions, we may earn income from advisory services; however, we had no income from advisory services in the three months ended March 31, 2018 or 2017.

Operating Expenses

Our operating expenses are comprised of interest and fees on our borrowings, general and administrative expenses and employee compensation and benefits. Our operating expenses totaled approximately $22.6 million and $23.7 million during the three months ended March 31, 2018 and 2017, respectively.

Interest and Fees on our Borrowings

Interest and fees on our borrowings totaled approximately $10.6 million and $12.4 million for the three months ended March 31, 2018 and 2017, respectively. Interest and fee expense for the three months ended March 31, 2018, as compared to March 31, 2017, decreased due to the partial redemption of our 2024 Notes and the redemption of our 2019 Notes in February 2017, which resulted in a one-time, non-cash acceleration of our unamortized fees and a thirty day interest overlap related to our Convertible Note issuance in January 2017.

We had a weighted average cost of debt, comprised of interest and fees, of approximately 5.3% and 6.3% for the three months ended March 31, 2018 and 2017, respectively. The decrease in the weighted average cost of debt for the three months ended March 31, 2018 as compared to the same period ended March 31, 2017 is primarily attributable to the redemption of our 2019 Notes between periods.

General and Administrative Expenses

General and administrative expenses include legal fees, consulting fees, accounting fees, printer fees, insurance premiums, rent, expenses associated with the workout of underperforming investments and various other expenses. Our general and administrative expenses decreased to $4.0 million from $4.1 million for the three months ended March 31, 2018 and 2017. The decrease for the three months ended March 31, 2018 was primarily attributable to a reduction in corporate legal and other expenses.

Employee Compensation

Employee compensation and benefits totaled $5.8 million for the three months ended March 31, 2018 as compared to $5.3 million for the three months ended March 31, 2017. The increase between the comparative periods was primarily due to increased salaries and changes in variable compensation expenses due to company performance objectives.

Employee stock-based compensation totaled $2.3 million for the three months ended March 31, 2018 as compared to $1.8 million for the three months ended March 31, 2017. The increase for the three-month comparative period was primarily related to restricted stock award vesting.

Net Investment Realized Gains and Losses and Net Unrealized Appreciation and Depreciation

Realized gains or losses are measured by the difference between the net proceeds from the repayment or sale and the cost basis of an investment without regard to unrealized appreciation or depreciation previously recognized, and includes investments written off during the period, net of recoveries. Net change in unrealized appreciation or depreciation primarily reflects the change in portfolio investment values during the reporting period, including the reversal of previously recorded unrealized appreciation or depreciation when gains or losses are realized.

A summary of realized gains and losses for the three months ended March 31, 2018 and 2017 is as follows:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Realized gains	$1,108	$6,470
Realized losses	(6,028)	(3,233)
Net realized gains (losses)	$(4,920)	$3,237

During the three months ended March 31, 2018 we recognized net realized losses of $4.9 million. During the three months ended March 31, 2018, we recorded gross realized gains of $1.1 million primarily from the sale or acquisition of our holdings. These gains were offset by gross realized losses of $6.0 million primarily from the liquidation or write-off of our warrant and equity investments in six portfolio companies and our debt investments in two portfolio companies.

During the three months ended March 31, 2017, we recognized net realized gains of $3.2 million. During the three months ended March 31, 2017, we recorded gross realized gains of $6.4 million primarily from the sale of our holdings in three portfolio companies. These gains were offset by gross realized losses of $3.2 million primarily from the liquidation or write-off of our warrant and equity investments in two portfolio companies and the sale of our public bond position in one portfolio company.

The following table summarizes the change in net unrealized appreciation/depreciation of investments for the three months ended March 31, 2018 and 2017:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Gross unrealized appreciation on portfolio investments	$7,797	$19,478
Gross unrealized depreciation on portfolio investments	(29,548)	(48,270)
Reversal of prior period net unrealized appreciation (depreciation) upon a realization event	6,666	(2,405)
Net unrealized appreciation (depreciation) on debt, equity, and warrant investments	(15,085)	(31,197)
Other net unrealized appreciation (depreciation)	(112)	(306)
Total net unrealized depreciation on investments	$(15,197)	$(31,503)

During the three months ended March 31, 2018, we recorded $15.2 million of net unrealized depreciation, of which $15.1 million was net unrealized depreciation from our debt, equity and warrant investments. We recorded $8.3 million of net unrealized depreciation on our debt investments which was primarily related to $13.5 million of unrealized depreciation on the debt portfolio including $9.0 million of unrealized depreciation on collateral-based impairments on seven portfolio companies. This unrealized depreciation was partially offset by $5.2 million of unrealized appreciation primarily due to the reversal of unrealized depreciation upon write-off of two portfolio companies.

We recorded $4.1 million of net unrealized depreciation on our equity investments and $2.7 million of net unrealized depreciation on our warrant investments during the three months ended March 31, 2018. This net unrealized depreciation of $6.8 million was due to $8.2 million of unrealized depreciation on the equity and warrant portfolio partially offset by $1.4 million of unrealized appreciation primarily due to the reversal of unrealized depreciation upon being realized as a gain or loss due to the acquisition or liquidation of our equity and warrant investments.

During the three months ended March 31, 2017, we recorded $31.5 million of net unrealized depreciation, of which $31.2 million was net unrealized depreciation from our debt, equity and warrant investments. We recorded $31.2 million of net unrealized depreciation on our debt investments, which was primarily related to $39.8 million of unrealized depreciation for collateral-based impairments on ten portfolio companies offset by the reversal of $3.2 million unrealized depreciation for the prior period collateral-based impairments on one portfolio company.

We recorded $2.8 million of net unrealized depreciation on our equity investments primarily due to the reversal of approximately $4.7 million of unrealized appreciation for one portfolio company upon being realized as a gain. We also recorded $2.8 million of net unrealized appreciation on our warrant investments during the three months ended March 31, 2017.

Income and Excise Taxes

We account for income taxes in accordance with the provisions of Topic 740 of the FASB’s Accounting Standards Codification, as amended (“ASC”), “Income Taxes”, under which income taxes are provided for amounts currently payable and for amounts deferred based upon the estimated future tax effects of differences between the financial statements and tax basis of assets and liabilities given the provisions of the enacted tax law. Valuation allowances may be used to reduce deferred tax assets to the amount likely to be realized. Based upon our previous election and anticipated continued qualification to be subject to taxation as a RIC, we are typically not subject to a material level of federal income taxes. We intend to distribute 100% of our spillover earnings from ordinary income for our taxable year ended December 31, 2017 to our stockholders in 2018.

Net Change in Net Assets Resulting from Operations and Earnings Per Share

For the three months ended March 31, 2018 we had a net increase in net assets resulting from operations of approximately $5.9 million and for the three months ended March 31, 2017 we had a net decrease in net assets resulting from operations of approximately $5.6 million.

Both the basic and fully diluted net change in net assets per common share were $0.07 per share for the three months ended March 31, 2018. Both the basic and fully diluted net change in net assets per common share were $(0.07) per share for the three months ended March 31, 2017.

For the purpose of calculating diluted earnings per share for three months ended March 31, 2018 and 2017, the effect of the 2022 Convertible Notes, outstanding options, and restricted stock units under the treasury stock method was considered. The effect of the 2022 Convertible Notes was excluded from these calculations for the three months ended March 31, 2018 and 2017 as our share price was less than the conversion price in effect which results in anti-dilution.

Financial Condition, Liquidity, and Capital Resources

Our liquidity and capital resources are derived from our SBA debentures, 2022 Notes, 2024 Notes, 2021 Asset-Backed Notes, 2022 Convertible Notes, Credit Facilities and cash flows from operations, including investment sales and repayments, and income earned. Our primary use of funds from operations includes investments in portfolio companies and payments of fees and other operating expenses we incur. We have used, and expect to continue to use, our borrowings and the proceeds from the turnover of our portfolio and from public and private offerings of securities to finance our investment objectives. We may also raise additional equity or debt capital through registered offerings off a shelf registration, At-The-Market ("ATM") and private offerings of securities, by securitizing a portion of our investments, or by borrowing from the SBA through our SBIC subsidiaries.

On August 16, 2013, we entered into an ATM equity distribution agreement (the "Prior Equity Distribution Agreement") with JMP Securities LLC ("JMP"). On March 7, 2016, we renewed the Prior Equity Distribution Agreement and on December 21, 2016, we further amended the agreement to increase the total shares available under the program. The Prior Equity Distribution Agreement, as amended, provided that we may offer and sell up to 12.0 million shares of our common stock from time to time through JMP, as our sales agent.

On September 7, 2017, we terminated the Prior Equity Distribution Agreement and entered into a new ATM equity distribution agreement (the "Equity Distribution Agreement") with JMP. As a result, the remaining shares that were available under the Prior Equity Distribution agreement are no longer available for issuance. The Equity Distribution Agreement provides that the Company may offer and sell up to 12.0 million shares of its common stock from time to time through JMP, as its sales agent. Sales of the Company's common stock, if any, may be made in negotiated transactions or transactions that are deemed to be "at the market," as defined in Rule 415 under the Securities Act, including sales made directly on the NYSE or similar securities exchange or sales made to or through a market maker other than on an exchange, at prices related to the prevailing market prices or at negotiated prices.

During the three months ended March 31, 2018, we sold 478,000 shares of common stock, which were issued under the Equity Distribution Agreement, for a total accumulated net proceeds of approximately $6.0 million, including $312,000 of offering expenses. As of March 31, 2018, approximately 9.9 million shares remain available for issuance and sale under the Equity Distribution Agreement. See " – Subsequent Events."

Our 2016 Convertible Notes were fully settled on or before their contractual maturity date of April 15, 2016. Throughout the life of the 2016 Convertible Notes, holders of approximately $74.8 million of our 2016 Convertible Notes exercised their conversion rights. These 2016 Convertible Notes were settled with a combination of cash equal to the outstanding principal amount of the converted notes and approximately 1.6 million shares of our common stock, or $24.3 million.

On May 2, 2016, we closed an underwritten public offering of an additional $72.9 million in aggregate principal amount of our 2024 Notes. The $72.9 million in aggregate principal amount includes $65.4 million from the initial offering on April 21, 2016 and $7.5 million as a result of underwriters exercising a portion of their option to purchase up to an additional $9.8 million in aggregate principal to cover overallotments on April 29, 2016. On June 27, 2016, we closed an underwritten public offering of an additional $60.0 million in aggregate principal amount of the 2024 Notes. On June 30, 2016, the underwriters exercised their option to purchase up to an additional $9.0 million in aggregate principal to cover overallotments, resulting in total aggregate principal of $69.0 million from the offering. The 2024 Notes rank equally in right of payment and form a single series of notes.

On May 5, 2016, we, through a special purpose wholly-owned subsidiary, Hercules Funding III, as borrower, entered into the credit facility (the "Union Bank Facility") with MUFG Union Bank, as the arranger and administrative agent, and the lenders party to the Union Bank Facility from time to time. The Union Bank Facility replaced our credit facility (the “Prior Union Bank Facility”) entered into on August 14, 2014 (as amended and restated from time to time) with MUFG Union Bank, as the arranger and administrative agent, and the lenders party to the Prior Union Bank Facility from time to time. Any references to amounts related to the Union Bank Facility prior to May 5, 2016 were incurred and relate to the Prior Union Bank Facility.

On October 11, 2016, we entered into a debt distribution agreement, pursuant to which we may offer for sale, from time to time, up to $150.0 million in aggregate principal amount of 2024 Notes through FBR Capital Markets & Co. acting as our sales agent. Sales of the 2024 Notes, if any, may be made in negotiated transactions or transactions that are deemed to be “at the market offerings” as defined in Rule 415 under the Securities Act, including sales made directly on the NYSE, or similar securities exchange or sales made through a market maker other than on an exchange at prices related to prevailing market prices or at negotiated prices.

We did not sell any notes under the program during the three months ended March 31, 2018. During the year ended December 31, 2017, we sold 225,457 notes for approximately $5.6 million in aggregate principal amount. As of March 31, 2018, approximately $136.4 million in aggregate principal amount remains available for issuance and sale under the debt distribution agreement.

On January 25, 2017, we issued $230.0 million in aggregate principal amount of 2022 Convertible Notes, which amount includes the additional $30.0 million aggregate principal amount issued pursuant to the initial purchaser's exercise in full of its overallotment option. The sale generated net proceeds of approximately $225.5 million, including $4.5 million of debt issuance costs. Aggregate issuances costs include the initial purchaser's discount of approximately $5.2 million, offset by the reimbursement of $1.2 million by the initial purchaser.

On February 24, 2017, we redeemed the $110.4 million remaining outstanding balance of our 2019 Notes in full.

On October 23, 2017, we issued $150.0 million in aggregate principal amount of the 2022 Notes. The 2022 Notes were issued pursuant to the Fourth Supplemental Indenture to the Base Indenture, dated October 23, 2017 (the "2022 Notes Indenture"), between us and U.S. Bank, National Association, as trustee (the "2022 Trustee"). The sale of the 2022 Notes generated net proceeds of approximately $147.5 million, including a public offering discount of $826,500. Aggregate estimated offering expenses in connection with the transaction, including the underwriter's discount and commissions of approximately $975,000, were approximately $1.7 million.

On November 23, 2017, we redeemed $75.0 million of the $258.5 million issued and outstanding aggregate principal amount of our 2024 Notes. On April 2, 2018, we redeemed an additional $100.0 million of the remaining outstanding aggregate principal amount of the 2024 Notes.

At March 31, 2018, we had $190.2 million of SBA debentures, $150.0 million of 2022 Notes, $183.5 million of 2024 Notes, $33.6 million of 2021 Asset-Backed Notes, and $230.0 million of 2022 Convertible Notes payable. We had no borrowings outstanding under the Wells Facility or the Union Bank Facility.

At March 31, 2018, we had $313.2 million in available liquidity, including $118.2 million in cash and cash equivalents. We had available borrowing capacity of $120.0 million under the Wells Facility and $75.0 million under the Union Bank Facility, both subject to existing terms and advance rates and regulatory requirements. We primarily invest cash on hand in interest bearing deposit accounts.

At March 31, 2018, we had $118.5 million of capital outstanding in restricted accounts related to our SBIC that we may use to fund new investments in the SBIC. With our net investments of $44.0 million and $74.5 million in HT II and HT III, respectively, we have the combined capacity to issue a total of $190.2 million of SBA guaranteed debentures, subject to SBA approval. At March 31, 2018, we have issued $190.2 million in SBA guaranteed debentures in our SBIC subsidiaries.

At March 31, 2018, we had approximately $3.6 million of restricted cash, which consists of collections of interest and principal payments on assets that are securitized. In accordance with the terms of the related securitized 2021 Asset-Backed Notes, based on current characteristics of the securitized debt investment portfolios, the restricted funds may be used to pay monthly interest and principal on the securitized debt and are not distributed to us or available for our general operations.

During the three months ended March 31, 2018, we principally funded our operations from (i) cash receipts from interest, dividend and fee income from our investment portfolio and (ii) cash proceeds from the realization of portfolio investments through the repayments of debt investments and the sale of debt and equity investments.

During the three months ended March 31, 2018, our operating activities provided $63.0 million of cash and cash equivalents, compared to $11.7 million provided during the three months ended March 31, 2017. This $51.3 million increase in cash provided by operating activities is primarily related to an increase in investment repayments of $138.4 million and an increase in net realized losses on investments of $8.2 million, partially offset by an increase in investment purchases of $82.6 million and a decrease in net unrealized depreciation of $16.3 million.

During the three months ended March 31, 2018, our investing activities used approximately $72,000 of cash, compared to $39,000 used during the three months ended March 31, 2017.

During the three months ended March 31, 2018, our financing activities used $36.1 million of cash, compared to $128.0 million provided during the three months ended March 31, 2017. The $164.1 million decrease in cash provided by financing activities was primarily due to a decrease in the issuance of our common stock under the equity distribution agreement of $41.0 million, the net issuance of $225.5 million of the 2022 Convertible Notes, offset by the repayment of $110.4 million of 2019 Notes during the three months ended March 31, 2017.

As of March 31, 2018, net assets totaled $828.7 million, with a NAV per share of $9.72. We intend to continue to operate in order to generate cash flows from operations, including income earned from investments in our portfolio companies. Our primary use of funds will be investments in portfolio companies and cash distributions to holders of our common stock.

As required by the 1940 Act, our asset coverage must be at least 200% (or 150%, subject to certain approval and disclosure requirements) after each issuance of senior securities. As of March 31, 2018 our asset coverage ratio under our regulatory requirements as a business development company was 238.2% excluding our SBA debentures as a result of our exemptive order from the SEC that allows us to exclude all SBA leverage from our asset coverage ratio. As a result of the SEC exemptive order, our ratio of total assets on a consolidated basis to outstanding indebtedness may be less than 200% (or 150%, subject to certain approval and disclosure requirements), which while providing increased investment flexibility, also may increase our exposure to risks associated with leverage. Total asset coverage ratio when including our SBA debentures was 204.8% at March 31, 2018.

Outstanding Borrowings

At March 31, 2018 and December 31, 2017, we had the following available borrowings and outstanding amounts:

	March 31, 2018			December 31, 2017		
(in thousands)	Total Available	Principal	Carrying Value (1)	Total Available	Principal	Carrying Value (1)
SBA Debentures (2)	$190,200	$190,200	$188,299	$190,200	$190,200	$188,141
2022 Notes	150,000	150,000	147,698	150,000	150,000	147,572
2024 Notes	183,510	183,510	179,161	183,510	183,510	179,001
2021 Asset-Backed Notes	33,575	33,575	33,156	49,153	49,153	48,650
2022 Convertible Notes	230,000	230,000	223,878	230,000	230,000	223,488
Wells Facility (3)	120,000	—	—	120,000	—	—
Union Bank Facility (3)	75,000	—	—	75,000	—	—
Total	$982,285	$787,285	$772,192	$997,863	$802,863	$786,852

(1) Except for the Wells Facility and Union Bank Facility, all carrying values represent the principal amount outstanding less the remaining unamortized debt issuance costs and unaccreted discount, if any, associated with the loan as of the balance sheet date. See below for the amount of debt issuance cost associated with each borrowing.
(2) At both March 31, 2018 and December 31, 2017, the total available borrowings under the SBA debentures were $190.2 million, of which $41.2 million was available in HT II and $149.0 million was available in HT III.
(3) Availability subject to us meeting the borrowing base requirements.

Debt issuance costs are fees and other direct incremental costs we incur in obtaining debt financing and are recognized as prepaid expenses and amortized over the life of the related debt instrument using the effective yield method or the straight line method, which closely approximates the effective yield method. In accordance with ASC Subtopic 835-30 ("Interest – Imputation of Interest"), debt issuance costs are presented as a reduction to the associated liability balance on the Consolidated Statement of Assets and Liabilities, except for debt issuance costs associated with line-of-credit arrangements. Debt issuance costs, net of accumulated amortization, as of March 31, 2018 and December 31, 2017 were as follows:

(in thousands)	March 31, 2018	December 31, 2017
SBA Debentures	$1,901	$2,059
2022 Notes	1,548	1,633

2024 Notes	4,417	4,591
2021 Asset-Backed Notes	420	503
2022 Convertible Notes	3,492	3,715
Wells Facility (1)	726	227
Union Bank Facility (1)	306	379
Total	$12,810	$ 13,107

(1) As the Wells Facility and Union Bank Facility are line-of-credit arrangements, the debt issuance costs associated with these instruments are presented separately as an asset on the Consolidated Statement of Assets and Liabilities in accordance with ASC Subtopic 835-30.

Refer to "Note 4 – Borrowings" included in the notes to our consolidated financial statements appearing elsewhere in this report for a discussion of the contract terms, interest expense, and fees associated with each outstanding borrowing as of and for the three months ended March 31, 2018.

Commitments

In the normal course of business, we are party to financial instruments with off-balance sheet risk. These consist primarily of unfunded contractual commitments to extend credit, in the form of loans, to our portfolio companies. Unfunded contractual commitments to provide funds to portfolio companies are not reflected on our balance sheet. Our unfunded contractual commitments may be significant from time to time. A portion of these unfunded contractual commitments are dependent upon the portfolio company reaching certain milestones before the debt commitment becomes available. Furthermore, our credit agreements contain customary lending provisions which allow us relief from funding obligations for previously made commitments in instances where the underlying company experiences materially adverse events that affect the financial condition or business outlook for the company. These commitments will be subject to the same underwriting and ongoing portfolio maintenance as are the on-balance sheet financial instruments that we hold. Since these commitments may expire without being drawn upon, the total commitment amount does not necessarily represent future cash requirements. As such, our disclosure of unfunded contractual commitments includes only those which are available at the request of the portfolio company and unencumbered by milestones.

At March 31, 2018, we had approximately $51.9 million of unfunded commitments, including undrawn revolving facilities, which were available at the request of the portfolio company and unencumbered by milestones. We intend to use cash flow from normal and early principal repayments, and proceeds from borrowings and notes to fund these commitments.

We also had approximately $174.0 million of non-binding term sheets outstanding to three new companies, which generally convert to contractual commitments within approximately 90 days of signing. Non-binding outstanding term sheets are subject to completion of our due diligence and final investment committee approval process, as well as the negotiation of definitive documentation with the prospective portfolio companies. Not all non-binding term sheets are expected to close and do not necessarily represent future cash requirements.

The fair value of our unfunded commitments is considered to be immaterial as the yield determined at the time of underwriting is expected to be materially consistent with the yield upon funding, given that interest rates are generally pegged to market indices and given the existence of milestones, conditions and/or obligations imbedded in the borrowing agreements.

As of March 31, 2018, our unfunded contractual commitments available at the request of the portfolio company, including undrawn revolving facilities, and unencumbered by milestones are as follows:

(in thousands)

Portfolio Company	Unfunded Commitments [(1)]
Chemocentryx, Inc.	$ 10,000
Evernote Corporation	10,000
Proterra, Inc.	10,000
Impact Radius Holdings, Inc.	5,000
Wrike, Inc.	5,000
Achronix Semiconductor Corporation	5,000
Oak Street Health	5,000

Lithium Technologies, Inc.	878
Greenphire	500
Insurance Technologies Corp.	500
Total	$ 51,878

(1) Amount represents unfunded commitments, including undrawn revolving facilities, which are available at the request of the portfolio company. Amount excludes unfunded commitments which are unavailable due to the borrower having not met certain milestones.

Contractual Obligations

The following table shows our contractual obligations as of March 31, 2018:

	Payments due by period (in thousands)				
		Less than	1 - 3	3 - 5	After 5
Contractual Obligations [1]	Total	1 year	years	years	years
Borrowings [2][3][5]	$787,285	$151,975	$61,550	$490,250	$83,510
Operating Lease Obligations [4]	17,290	2,436	5,005	5,912	3,937
Total	$804,575	$154,411	$66,555	$496,162	$87,447

(1) Excludes commitments to extend credit to our portfolio companies.
(2) Includes $190.2 million in principal outstanding under the SBA debentures, $150.0 million of the 2022 Notes, $183.5 million of the 2024 Notes, $33.6 million of the 2021 Asset-Backed Notes and $230.0 million of the 2022 Convertible Notes as of March 31, 2018.
(3) Amounts represent future principal repayments and not the carrying value of each liability. See Note 4 to our consolidated financial statements.
(4) Facility leases and licenses.
(5) Reflects announced redemption of a portion of the 2024 Notes in April 2018. See " – Subsequent Events."

Certain premises are leased or licensed under agreements which expire at various dates through June 2027. Total rent expense amounted to approximately $451,000 and $444,000 during the three months ended March 31, 2018 and 2017 respectively.

Indemnification Agreements

We have entered into indemnification agreements with our directors and executive officers. The indemnification agreements are intended to provide our directors and executive officers the maximum indemnification permitted under Maryland law and the 1940 Act. Each indemnification agreement provides that we shall indemnify the director or executive officer who is a party to the agreement, or an "Indemnitee," including the advancement of legal expenses, if, by reason of his or her corporate status, the Indemnitee is, or is threatened to be, made a party to or a witness in any threatened, pending, or completed proceeding, to the maximum extent permitted by Maryland law and the 1940 Act.

We and our executives and directors are covered by Directors and Officers Insurance, with the directors and officers being indemnified by us to the maximum extent permitted by Maryland law subject to the restrictions in the 1940 Act.

Distributions

The following table summarizes our distributions declared and paid, to be paid, or reinvested on all shares, including restricted stock, to date:

Date Declared	Record Date	Payment Date	Amount Per Share
			$ 11.23

Cumulative distributions declared and paid prior to January 1, 2016			
February 17, 2016	March 7, 2016	March 14, 2016	0.31
April 27, 2016	May 16, 2016	May 23, 2016	0.31
July 27, 2016	August 15, 2016	August 22, 2016	0.31
October 26, 2016	November 14, 2016	November 21, 2016	0.31
February 16, 2017	March 6, 2017	March 13, 2017	0.31
April 26, 2017	May 15, 2017	May 22, 2017	0.31
July 26, 2017	August 14, 2017	August 21, 2017	0.31
October 25, 2017	November 13, 2017	November 20, 2017	0.31
February 14, 2018	March 5, 2018	March 12, 2018	0.31
April 25, 2018	May 14, 2018	May 21, 2018	0.31
			$ 14.33

On April 25, 2018, the Board of Directors declared a cash distribution of $0.31 per share to be paid on May 21, 2018 to stockholders of record as of May 14, 2018. This distribution represents our fifty-first consecutive distribution since our initial public offering, bringing the total cumulative distribution to date to $14.33 per share.

Our Board of Directors maintains a variable distribution policy with the objective of distributing four quarterly distributions in an amount that approximates 90 - 100% of our taxable quarterly income or potential annual income for a particular taxable year. In addition, at the end of our taxable year, our Board of Directors may choose to pay an additional special distribution, or fifth distribution, so that we may distribute approximately all of our annual taxable income in the taxable year in which it was earned, or may elect to maintain the option to spill over our excess taxable income into the following taxable year as part of any future distribution payments.

Distributions from our taxable income (including gains) to a stockholder generally will be treated as a dividend for U.S. federal income tax purposes to the extent of such stockholder's allocable share of our current or accumulated earnings and profits. Distributions in excess of our current and accumulated earnings and profits would generally be treated first as a return of capital to the extent of a stockholder's tax basis in our shares, and any remaining distributions would be treated as a capital gain. The determination of the tax attributes of our distributions is made annually as of the end of our taxable year based upon our taxable income for the full taxable year and distributions paid for the full taxable year. As a result, any determination of the tax attributes of our distributions made on a quarterly basis may not be representative of the actual tax attributes of the Company's distributions for a full taxable year. Of the distributions declared during the year ended December 31, 2017, 100% were distributions derived from our current and accumulated earnings and profits.

During the three months ended March 31, 2018, we declared a distribution of $0.31 per share. If we had determined the tax attributes of our distributions year-to-date as of March 31, 2018, 100% would be from our current and accumulated earnings and profits. However, there can be no certainty to stockholders that this determination is representative of what the tax attributes of our 2018 distributions to stockholders will actually be.

We maintain an "opt out" dividend reinvestment plan that provides for reinvestment of our distribution on behalf of our stockholders, unless a stockholder elects to receive cash. As a result, if our Board of Directors authorizes, and we declare a cash distribution, then our stockholders who have not "opted out" of our dividend reinvestment plan will have their cash distribution automatically reinvested in additional shares of our common stock, rather than receiving the cash distributions.

Shortly after the close of each calendar year information identifying the source of the distribution (i.e., paid from ordinary income, paid from net capital gains on the sale of securities, and/or a return of paid-in-capital surplus which is a nontaxable distribution, if any) will be provided to our stockholders subject to information reporting. To the extent our taxable earnings fall below the total amount of our distributions for any taxable year, a portion of those distributions may be deemed a tax return of capital to our stockholders.

We expect to qualify to be subject to tax as a RIC under Subchapter M of the Code. In order to be subject to tax as a RIC, we are required to satisfy certain annual gross income and quarterly asset composition tests, as well as make distributions to our stockholders each taxable year treated as dividends for federal income tax purposes of an amount at least equal to 90% of the sum of our investment company taxable income, determined without regard to any deduction for dividends paid, plus our net tax-exempt income, if any. Upon being eligible to be subject to tax as a RIC, we would be entitled to deduct such distributions we pay to our stockholders in determining the overall components of our "taxable income." Components of our taxable income include our taxable interest, dividend and fee income, reduced by certain deductions, as well as taxable net realized securities gains. Taxable income generally differs from net income for financial reporting purposes due to temporary and permanent differences in the recognition of income and expenses and generally excludes net unrealized appreciation or depreciation as such gains or losses are not included in taxable income until they are realized. In connection with maintaining our ability to be subject to tax as a RIC, among other things, we have made and intend to continue to make the requisite distributions to our stockholders each taxable year, which generally should relieve us from corporate-level U.S. federal income taxes.

As a RIC, we will be subject to a 4% nondeductible U.S. federal excise tax on certain undistributed income and gains unless we make distributions treated as dividends for U.S. federal income tax purposes in a timely manner to our stockholders in respect of each calendar year of an amount at least equal to the Excise Tax Avoidance Requirement. We will not be subject to this excise tax on any amount on which we incurred U.S. federal corporate income tax (such as the tax imposed on a RIC's retained net capital gains).

Depending on the level of taxable income earned in a taxable year, we may choose to carry over taxable income in excess of current taxable year distributions treated as dividends for U.S. federal income tax purposes from such taxable income into the next taxable year and incur a 4% excise tax on such taxable income, as required. The maximum amount of excess taxable income that may be carried over for distribution in the next taxable year under the Code is the total amount of distributions treated as dividends for U.S. federal income tax purposes paid in the following taxable year, subject to certain declaration and payment guidelines. To the extent we choose to carry over taxable income into the next taxable year, distributions declared and paid by us in a taxable year may differ from our taxable income for that taxable year as such distributions may include the distribution of current taxable year taxable income, the distribution of prior taxable year taxable income carried over into and distributed in the current taxable year, or returns of capital.

We can offer no assurance that we will achieve results that will permit the payment of any cash distributions and, if we issue senior securities, we will be prohibited from making distributions if doing so causes us to fail to maintain the asset coverage ratios stipulated by the 1940 Act or if distributions are limited by the terms of any of our borrowings. Our ability to make distributions will be limited by the asset coverage requirements under the 1940 Act.

We intend to distribute 100% of our spillover earnings, which consists of ordinary income, from the year ended December 31, 2017 to our stockholders during 2018.

Critical Accounting Policies

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles ("U.S. GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and revenues and expenses during the period reported. On an ongoing basis, our management evaluates its estimates and assumptions, which are based on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results could differ from those estimates. Changes in our estimates and assumptions could materially impact our results of operations and financial condition.

Reclassification

Certain balances from prior years have been reclassified in order to conform to the current year presentation.

Valuation of Investments

The most significant estimate inherent in the preparation of our consolidated financial statements is the valuation of investments and the related amounts of unrealized appreciation and depreciation of investments recorded.

At March 31, 2018, approximately 91.6% of our total assets represented investments in portfolio companies whose fair value is determined in good faith by the Board of Directors. Value, as defined in Section 2(a)(41) of the 1940 Act, is (i) the market price for those securities for which a market quotation is readily available and (ii) for all other securities and assets, fair value is as determined in good faith by the Board of Directors. Our investments are carried at fair value in accordance with the 1940 Act and ASC Topic 946 and measured in accordance with ASC Topic 820. Our debt securities are primarily invested in venture capital-backed companies in technology-related industries including technology, drug discovery and development, biotechnology, life sciences, healthcare and sustainable and renewable technology at all stages of development. Given the nature of lending to these types of businesses, substantially all of our investments in these portfolio companies are considered Level 3 assets under ASC Topic 820 because there is no known or accessible market or market indexes for these investment securities to be traded or exchanged. As such, we value substantially all of our investments at fair value as determined in good faith pursuant to a consistent valuation policy by our Board of Directors in accordance with the provisions of ASC Topic 820 and the 1940 Act. Due to the inherent uncertainty in determining the fair value of investments that do not have a readily available market value, the fair value of our investments determined in good faith by our Board of Directors may differ significantly from the value that would have been used had a readily available market existed for such investments, and the differences could be material.

We may from time to time engage an independent valuation firm to provide us with valuation assistance with respect to certain of our portfolio investments. We engage independent valuation firms on a discretionary basis. Specifically, on a quarterly basis, we will identify portfolio investments with respect to which an independent valuation firm will assist in valuing. We select these portfolio investments based on a number of factors, including, but not limited to, the potential for material fluctuations in valuation results, credit quality and the time lapse since the last valuation of the portfolio investment by an independent valuation firm.

We intend to continue to engage an independent valuation firm to provide us with assistance regarding our determination of the fair value of selected portfolio investments each quarter unless directed by the Board of Directors to cancel such valuation services. The scope of the services rendered by an independent valuation firm is at the discretion of the Board of Directors. Our Board of Directors is ultimately, and solely, responsible for determining the fair value of our investments in good faith.

Refer to “Note 2 – Summary of Significant Accounting Policies” included in the notes to our consolidated financial statements appearing elsewhere in this report for a discussion of our valuation policies for the three months ended March 31, 2018.

Income Recognition

See “— Changes in Portfolio” for a discussion of our income recognition policies and results during the three months ended March 31, 2018. See “— Results of Operations” for a comparison of investment income for the three months ended March 31, 2018 and 2017.

Stock Based Compensation

We have issued and may, from time to time, issue stock options and restricted stock to employees under our 2004 Equity Incentive Plan and to Board members under our 2006 Equity Incentive Plan prior to its expiration on June 21, 2017. We follow the guidelines set forth under ASC Topic 718, ("Compensation – Stock Compensation") to account for stock options granted. Under ASC Topic 718, compensation expense associated with stock-based compensation is measured at the grant date based on the fair value of the award and is recognized over the vesting period. Determining the appropriate fair value model and calculating the fair value of stock-based awards at the grant date requires judgment, including estimating stock price volatility, forfeiture rate and expected option life.

Recent Accounting Pronouncements

In January 2016, the FASB issued Accounting Standards Update ("ASU") 2016-01, "Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities," which, among other things, requires that (i) all equity investments, other than equity-method investments, in unconsolidated entities generally be measured at fair value through earnings and (ii) an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. Additionally, the ASU changes the disclosure requirements for financial instruments. ASU 2016-01 is effective for annual reporting periods, and the interim periods within those periods, beginning after December 15, 2017. We have adopted this standard, which did not have a material impact, on our consolidated financial statements and related disclosures for the periods presented.

In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)," which, among other things, requires recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous U.S. GAAP. Additionally, the ASU requires the classification of all cash payments on leases within operating activities in the Consolidated Statement of Cash Flows. ASU 2016-02 is effective for annual reporting periods, and the interim periods within those periods, beginning after December 15, 2018. Early adoption is permitted. We anticipate an increase in the recognition of right-of-use assets and lease liabilities, however, we do not believe that ASU 2016-02 will have a material impact on our consolidated financial statements and disclosures.

In August 2016, the FASB issued ASU 2016-15, "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments," which addresses eight specific cash flow issues including, among other things, the classification of debt prepayment or debt extinguishment costs. ASU 2016-15 is effective for annual reporting periods, and the interim periods within those periods, beginning after December 15, 2017. We have adopted this standard, which did not have a material impact, on our consolidated financial statements and related disclosures for the periods presented.

In October 2016, the SEC adopted new rules and forms and amended other rules to enhance the reporting and disclosure of information by registered investment companies. As part of these changes, the SEC amended Regulation S-X to standardize and enhance disclosures in investment company financial statements. Implementation of the new or amended rules is required for reporting periods ending after August 1, 2017. We have reviewed the requirements and adopted the amendments to Regulation S-X on our consolidated financial statements and related disclosures for the periods presented.

In November 2016, the FASB issued ASU 2016-18, "Statement of Cash Flows (Topic 230)," which requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The new guidance is effective for interim and annual periods beginning after December 15, 2017. We have adopted this standard, which did not have a material impact, on our consolidated financial statements and related disclosures for the periods presented.

Subsequent Events

Distribution Declaration

On April 25, 2018 the Board of Directors declared a cash distribution of $0.31 per share to be paid on May 21, 2018 to stockholders of record as of May 14, 2018. This distribution represents our fifty-first consecutive distribution since our initial public offering, bringing the total cumulative distribution to date to $14.33 per share.

Redemption of 2024 Notes

On February 9, 2018, our Board of Directors approved a redemption of $100.0 million of outstanding aggregate principal amount of the 2024 Notes, which were redeemed on April 2, 2018.

ATM Equity Program Issuances

Subsequent to March 31, 2018 and as of April 30, 2018, we sold 679,800 shares of common stock for total accumulated net proceeds of approximately $8.2 million, including $74,000 of offering expenses, under the Equity Distribution Agreement with JMP. As of April 30, 2018, approximately 9.2 million shares remain available for issuance and sale under the Equity Distribution Agreement.

2025 Notes

On April 26, 2018, we issued $75.0 million in aggregate principal amount of 5.25% notes due 2025 (the “2025 Notes”). The 2025 Notes were issued pursuant to the Fifth Supplemental Indenture to the Base Indenture, dated April 26, 2018 (the “2025 Notes Indenture”), between us and U.S. Bank, National Association, as trustee. The sale of the 2025 Notes generated net proceeds of approximately $73.0 million. Aggregate estimated offering expenses in connection with the transaction, including the underwriter’s discount and commissions, were approximately $2.0 million.

The 2025 Notes will mature on April 30, 2025, unless previously repurchased in accordance with their terms. The 2025 Notes bear interest at a rate of 5.25% per year payable quarterly in arrears on January 30, April 30, July 30 and October 30 of each year, commencing on July 30, 2018.

The 2025 Notes will be our direct unsecured obligations and rank pari passu, or equally in right of payment, with all outstanding and future unsecured unsubordinated indebtedness issued by Hercules Capital, Inc.

We may redeem some or all of the 2025 Notes at any time, or from time to time, at the redemption price set forth under the terms of the indenture after April 30, 2021. No sinking fund is provided for the 2025 Notes. The 2025 Notes were issued in denominations of $25 and integral multiples of $25 thereof.

The 2025 Notes are listed on the NYSE, and trade on the NYSE under the symbol “HCXZ.”

Portfolio Company Developments

As of April 30, 2018, we held warrants or equity positions in three companies that have filed registration statements on Form S-1 with the SEC in contemplation of potential initial public offerings. All three companies filed confidentially under the Jumpstart Our Business Startups Act of 2012, or the JOBS Act. There can be no assurance that companies that have yet to complete their initial public offerings will do so in a timely manner or at all. In addition, subsequent to March 31, 2018, the following companies announced or completed liquidity events:

1. In March 2018, our portfolio company IntegenX, Inc., the market leader of rapid human DNA identification technology for use in forensics and law enforcement applications, announced that they have been acquired by Thermo Fisher Scientific Inc., the world leader in serving science. Terms of the transaction were not disclosed.
2. In April 2018, our portfolio company, DocuSign, Inc. completed its initial public offering.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are subject to financial market risks, including changes in interest rates. Interest rate risk is defined as the sensitivity of our current and future earnings to interest rate volatility, variability of spread relationships, the difference in re-pricing intervals between our assets and liabilities and the effect that interest rates may have on our cash flows. Changes in interest rates may affect both our cost of funding and our interest income from portfolio investments, cash and cash equivalents and idle fund investments. Our investment income will be affected by changes in various interest rates, including LIBOR and Prime rates, to the extent our debt investments include variable interest rates. As of March 31, 2018, approximately 96.5% of the loans in our portfolio had variable rates based on floating Prime or LIBOR rates with a floor. Changes in interest rates can also affect, among other things, our ability to acquire and originate loans and securities and the value of our investment portfolio.

Based on our Consolidated Statement of Assets and Liabilities as of March 31, 2018, the following table shows the approximate annualized increase (decrease) in components of net assets resulting from operations of hypothetical base rate changes in interest rates, assuming no changes in our investments and borrowings.

(in thousands) Basis Point Change	Interest Income	Interest Expense	Net Income	EPS[(1)]
25	$3,088	$ —	$3,088	$0.04
50	$6,197	$ —	$6,197	$0.07
75	$9,394	$ —	$9,394	$0.11
100	$12,591	$ —	$12,591	$0.15
200	$25,791	$ —	$25,791	$0.30
300	$38,578	$ —	$38,578	$0.46

(1) Earnings per share impact calculated based on basic weighted average shares outstanding of 84,596.

We do not currently engage in any hedging activities. However, we may, in the future, hedge against interest rate fluctuations (and foreign currency) by using standard hedging instruments such as futures, options, and forward contracts. While hedging activities may insulate us against changes in interest rates (and foreign currency), they may also limit our ability to participate in the benefits of lower interest rates with respect to our borrowed funds and higher interest rates with respect to our portfolio of investments. During the three months ended March 31, 2018 we did not engage in interest rate (or foreign currency) hedging activities.

Although we believe that the foregoing analysis is indicative of our sensitivity to interest rate changes, it does not adjust for potential changes in the credit market, credit quality, size and composition of the assets in our portfolio. It also does not adjust for other business developments, including borrowings under our SBA debentures, 2022 Notes, 2024 Notes, 2021 Asset-Backed Notes, 2022 Convertible Notes and Credit Facilities that could affect the net increase in net assets resulting from operations, or net income. It also does not assume any repayments from borrowers. Accordingly, no assurances can be given that actual results would not differ materially from the statement above.

Because we currently borrow, and plan to borrow in the future, money to make investments, our net investment income is dependent upon the difference between the rate at which we borrow funds and the rate at which we invest the funds borrowed. Accordingly, there can be no assurance that a significant change in market interest rates will not have a material adverse effect on our net investment income. In periods of rising interest rates, our cost of funds would increase, which could reduce our net investment income if there is not a corresponding increase in interest income generated by variable rate assets in our investment portfolio.

For additional information regarding the interest rate associated with each of our, SBA debentures, 2022 Notes, 2024 Notes, 2021 Asset-Backed Notes, 2022 Convertible Notes, and Credit Facilities, please refer to “Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations - Financial Condition, Liquidity and Capital Resources - Outstanding Borrowings” in this quarterly report on Form 10-Q.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

Our chief executive and chief financial officers, under the supervision and with the participation of our management, conducted an evaluation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act. As of the end of the period covered by this quarterly report on Form 10-Q, our chief executive and chief financial officers have concluded that our disclosure controls and procedures were effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms, and that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our chief executive and chief financial officers, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

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

PART II: OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS
We may, from time to time, be involved in litigation arising out of our operations in the normal course of business or otherwise. Furthermore, third parties may try to seek to impose liability on us in connection with the activities of our portfolio companies. While the outcome of any current legal proceedings cannot at this time be predicted with certainty, we do not expect any current matters will materially affect our financial condition or results of operations; however, there can be no assurance whether any pending legal proceedings will have a material adverse effect on our financial condition or results of operations in any future reporting period.

ITEM 1A. RISK FACTORS
In addition to the risks discussed below, important risk factors that could cause results or events to differ from current expectations are described in Part I, Item 1A "Risk Factors" of the Company's Annual Report on Form 10-K for the year ended December 31, 2017 filed with the Securities and Exchange Commission on February 22, 2018.

Our financial results could be negatively affected if a significant portfolio investment fails to perform as expected.

Our total investment in companies may be significant individually or in the aggregate. As a result, if a significant investment in one or more companies fails to perform as expected, our financial results could be more negatively affected and the magnitude of the loss could be more significant than if we had made smaller investments in more companies. The following table shows the fair value of the totals of investments held in portfolio companies March 31, 2018 that represent greater than 5% of our net assets:

	March 31, 2018		
(in thousands)	Fair Value	Percentage of Net Assets	
Paratek Pharmaceuticals, Inc. (p.k.a. Transcept Pharmaceuticals, Inc.)	$60,893	7.3	%
Axovant Sciences Ltd.	53,842	6.5	%
Fuze, Inc.	50,418	6.1	%
Emma, Inc.	47,785	5.8	%
Snagajob.com, Inc.	42,572	5.1	%

- Paratek Pharmaceuticals, Inc. is a biopharmaceutical company focused on the development and commercialization of innovative therapies based upon its expertise in novel tetracycline chemistry
- Axovant Sciences Ltd. is a clinical-stage biopharmaceutical company focused on acquiring, developing and commercializing novel therapeutics for the treatment of dementia.
- Fuze, Inc. is a technology company that provides a cloud-based unified communications-as-a-service platform to server message block, mid-market, and small enterprise customers worldwide.
- Emma, Inc. is a technology company that offers software to enable organizations to create, send and track email marketing campaigns and online surveys.
- Snagajob.com, Inc. is a technology company that offers an array of services designed to simplify the hourly job recruiting process for both job seekers and employers.

Our financial results could be materially adversely affected if these portfolio companies or any of our other significant portfolio companies encounter financial difficulty and fail to repay their obligations or to perform as expected.

Recently passed legislation may allow us to incur additional leverage.

Historically, as a business development company, under the 1940 Act generally we are not permitted to incur indebtedness unless immediately after such borrowing we have an asset coverage for total borrowings of at least 200% (i.e., the amount of debt may not exceed 50% of the value of our assets). The Small Business Credit Availability Act, which was signed into law in March 2018, modifies this section of the 1940 Act and decreases this percentage from 200% to 150% (subject to either stockholder approval or approval of both a majority of the board of directors and a majority of directors who are not interested persons). As a result of this new law, we may be able to incur additional indebtedness subject to relevant approval and disclosure requirements and, therefore, your risk of an investment in us may increase. Rating agencies may also decide to review our credit ratings and those of other business development companies in light of this new law as well as any corresponding changes to asset coverage ratios and consider downgrading such ratings, including a downgrade from an investment grade rating to a non-investment grade rating. Such a downgrade in our credit ratings may adversely affect our other securities.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Dividend Reinvestment Plan

During the three months ended March 31, 2018, we issued 34,758 shares of common stock to stockholders in connection with the dividend reinvestment plan. These issuances were not subject to the registration requirements of the Securities Act. The aggregate value of the shares of our common stock issued under our dividend reinvestment plan was approximately $426,000.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable

ITEM 5. OTHER INFORMATION

2018 Annual Meeting

We have not yet announced the date for our 2018 annual meeting of stockholders (the “2018 Annual Meeting”). Because we expect that the 2018 Annual Meeting date will represent a change of more than thirty days from the anniversary of our 2017 annual meeting of stockholders held on December 13, 2017, the deadline for the receipt of stockholder proposals for the 2018 Annual Meeting will change. When we set the date for our 2018 Annual Meeting, we will publicly announce such data and deadlines for the receipt of stockholder proposals.

Retention Performance Stock Units and Cash Retention Bonus Awards

On May 2, 2018, the Company granted long-term Retention Performance Stock Unit awards (the “Retention PSUs”) under its 2004 Equity Incentive Plan to Manuel Henriquez and Scott Bluestein, and separate cash bonus awards with similar terms (the “Cash Awards”) to Gerard Waldt and three other senior personnel. The awards are designed to provide incentives that increase along with the total shareholder return (“TSR”) and further align the interests of key management with those of the Company’s shareholders. The Company believes that there is a highly competitive market place for senior personnel that have the experience and track record of successfully sourcing, financing and managing the asset class in which the Company invests. Accordingly, the Compensation Committee and the other independent directors adopted this program with the assistance of F.W. Cook. These awards are intended to promote long term management consistency and retention and to mitigate the likelihood of departure to competitors of those individuals most responsible for delivering financial performance to our shareholders. The objectives are sought to be achieved by offering a four year cliff vesting retention program to reward critical executives and senior personnel, whose services are valuable to the Company and industry competitors as a result of their proven and specialized expertise sourcing and funding venture debt. The target number of Retention PSUs granted to Mr. Henriquez and Mr. Bluestein are 812,348 and 487,409, respectively. The target amount of the Cash Award granted to Mr. Waldt is $500,000, and $3,500,000, in the aggregate, for the three other senior personnel.

The Retention PSUs and Cash Awards do not vest until the fourth anniversary “cliff vest” of the grant date (or a change in control of the Company, if earlier) and the Retention PSUs must generally be held and not disposed of until the fifth anniversary of the grant date, except in the event of death, disability or a change in control. No Retention PSUs or Cash Awards will vest if the Company's TSR relative to certain specified publicly traded business development companies (BDCs) is not at or above the 25th percentile level of such BDCs. 50% of the target Cash Award and target number of Retention PSUs will vest if the Company's TSR performance relative to such BDCs is at the 25th percentile level. 100% of the target Cash Award and target number of Retention PSUs will vest if the Company's TSR performance relative to such BDCs is at the 50th percentile level. 200% of the target Cash Award and target number of Retention PSUs will vest if the Company's TSR performance relative to such BDCs is at the 90th percentile level. If the Company's TSR performance is between the 25th percentile and the 50th percentile, or between the 50th percentile and the 90th percentile, of such BDCs, the amount of the Cash Awards vested and payable and the number of vested and payable Retention PSUs will be determined by linear interpolation between the foregoing metrics. Dividend equivalents will accrue in respect only of the Retention PSUs in the form of additional Retention PSUs, but will not be paid unless the Retention PSUs to which such dividend equivalents relate actually vest. The Cash Awards are not eligible to accrue dividend equivalents. TSR is calculated assuming dividend reinvestment and measurement begins on the date of grant and utilizes a 20 trading day volume weighted average price ending on the last trading day of the four year TSR performance period.

In the event of death or disability occurring prior to the fourth anniversary of the date of grant, Retention PSUs and the Cash Awards will vest, along with, in the case only of the Retention PSUs, any accrued dividend equivalents, on the date of such death or disability, with the Relative TSR Percentile Rank used to calculate such vesting to be the greater of (a) 50% and (b) the actual Relative TSR Percentile Rank as of the date of such death or disability. In the event of a voluntary termination prior to the fourth anniversary, all Cash Awards and Retention PSUs, and accrued dividend equivalents, will be forfeited. In the event of an involuntary termination without Cause prior to the fourth anniversary of the date of grant, the Retention PSUs and Cash Awards will be pro-rated based on service through the date of termination and such pro-rated Retention PSUs and Cash Awards will vest based on the actual relative TSR performance over the four year TSR performance period. In the event of a termination for Cause occurring at any time prior to delivery of the shares underlying the Retention PSUs or payment of the Cash Awards, all Retention PSUs and accrued dividend equivalents, and Cash Awards will be forfeited.

In the event of a change in control of the Company, Retention PSUs and Cash Awards will vest and be paid on a non-pro-rated basis based on the actual relative TSR performance through the date of the change in control utilizing the transaction price for the Company and the peer group TSR through the date of the change in control.

ITEM 6. EXHIBITS

Exhibit Number	Description
10.1*	Form of Retention Performance Stock Unit Award Agreement.
10.2*	Form of Cash Retention Bonus Award Agreement.
11	Computation of Per Share Earnings (included in Note 8 to the Consolidated Financial Statements included in this report).
31.1*	Chief Accounting Officer Certification Pursuant to Exchange Act Rule 13a-14 (a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Chief Accounting Officer Certification Pursuant to Exchange Act Rule 13a-14 (a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Chief Executive Officer Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2*	Chief Accounting Officer Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

*Filed herewith.

Schedule 12 – 14

HERCULES CAPITAL, INC.

SCHEDULE OF INVESTMENTS IN AND ADVANCES TO AFFILIATES

For the Three Months Ended March 31, 2018

(in thousands)

Portfolio Company	Investment [1]	Amount of Interest Credited to Income [2]	Realized Gain (Loss)	As of December 31, 2017 Fair Value	Gross Additions [3]	Gross Reductions [4]	Net Change in Unrealized Appreciation/ (Depreciation)	As of March 31, 2018 Fair Value
Control Investments								
Majority Owned Control Investments								
Achilles Technology Management Co II, Inc.	Common Stock	$ —	$ —	$ 242	$ —	$ —	$ (125)	$ 117
Gibraltar Business Capital, LLC [8]	Senior Debt	127	—	—	9,802	—	—	9,802
	Preferred Stock	—	—	—	25,538	—	—	25,538
	Common Stock	—	—	—	1,861	—	—	1,861
Total Majority Owned Control Investments		$ 127	$ —	$ 242	$ 37,201	$ —	$ (125)	$ 37,318
Other Control Investments								
Second Time Around (Simplify Holdings, LLC) [7]	Senior Debt	$ —	$ (1,743)	$ —	$ —	$ (1,781)	$ 1,781	$ —
Tectura Corporation[5]	Senior Debt	459	335	19,219	487	(335)	(2,276)	17,095
	Preferred Stock	—	—	—	—	—	—	—
Total Other Control Investments		$ 459	$ (1,408)	$ 19,219	$ 487	$ (2,116)	$ (495)	$ 17,095
Total Control Investments		$ 586	$ (1,408)	$ 19,461	$ 37,688	$ (2,116)	$ (620)	$ 54,413
Affiliate Investments								
Optiscan BioMedical, Corp.	Preferred Warrants	$ —	$ —	$ 86	$ —	$ —	$ 185	$ 271
	Preferred Stock	—	—	6,205	1,301	—	(1,250)	6,256
Solar Spectrum Holdings LLC	Senior Debt	561	—	13,604	166	(2,000)	(87)	11,683

(p.k.a. Sungevity, Inc.)(6)								
	Common Stock	—	—	11,400	—	—	915	12,315
Stion Corporation	Preferred Warrants	—	—	—	—	—	—	—
Total Affiliate Investments		$ 561	$—	$ 31,295	$ 1,467	$ (2,000)	$ (237)	$ 30,525
Total Control and Affiliate Investments		$ 1,147	$ (1,408)	$ 50,756	$ 39,155	$ (4,116)	$ (857)	$ 84,938

(1) Stock and warrants are generally non-income producing and restricted.

(2) Represents the total amount of interest or dividends credited to income for the period an investment was an affiliate or control investment.

(3) Gross additions include increases in the cost basis of investments resulting from new portfolio investments, paid-in-kind interest or dividends, the amortization of discounts and closing fees and the exchange of one or more existing securities for one or more new securities.

(4) Gross reductions include decreases in the cost basis of investments resulting from principal repayments or sales and the exchange of one or more existing securities for one or more new securities. Gross reductions also include previously recognized depreciation on investments that become control or affiliate investments during the period.

(5) As of March 31, 2017, the Company's investment in Tectura Corporation became classified as a control investment as of result of obtaining more than 50% representation on the portfolio company's board.

(6) As of September 30, 2017, the Company's investment in Solar Spectrum Holdings LLC (p.k.a. Sungevity, Inc.) became classified as an affiliate investment due to a reduction in equity ownership. Note that this investment was classified as a control investment as of June 30, 2017 after the Company obtained a controlling financial interest.

(7) As of February 2018, the Company’s investments in Second Time Around ((Simplify Holdings, LLC) were deemed wholly worthless and written off for a realized loss.

(8) As of March 31, 2018, the Company's investment in Gibraltar Business Capital, LLC became classified as a control investment as a result of obtaining a controlling financial interest

Schedule 12 – 14

HERCULES CAPITAL, INC.

SCHEDULE OF INVESTMENTS IN AND ADVANCES TO AFFILIATES

As of March 31, 2018

(in thousands)

Portfolio Company	Industry	Type of Investment (1)	Maturity Date	Interest Rate and Floor	Principal or Shares	Cost	Value (2)
Control Investments							
Majority Owned Control Investments							
Achilles Technology Management Co II, Inc.	Communications & Networking	Common Stock			100	$3,100	$117
Gibraltar Business Capital, LLC	Diversified Financial Services	Unsecured Debt	March 2023	Interest rate FIXED 14.50%	$10,000	9,802	9,802
	Diversified Financial Services	Preferred Stock			10,602,752	25,538	25,538
	Diversified Financial Services	Common Stock			830,000	1,861	1,861
Total Gibraltar Business Capital, LLC						$37,201	$37,201
Total Majority Owned Control Investments (4.51%)*						$40,301	$37,318
Other Control Investments							
Tectura Corporation	Internet Consumer & Business Services	Senior Secured Debt	June 2021	Interest rate FIXED 6.00%, PIK Interest 3.00%	$20,450	$20,450	$17,095
	Internet Consumer & Business Services	Senior Secured Debt	June 2021	PIK Interest 8.00%	$10,680	240	—
	Internet Consumer & Business Services	Preferred Series BB Equity			1,000,000	—	—
Total Tectura Corporation						20,690	17,095

Total Other Control Investments (2.06%)*						$20,690	$17,095
Total Control Investments (6.57%)*						$60,991	$54,413
Affiliate Investments							
Optiscan BioMedical, Corp.	Medical Devices & Equipment	Preferred Series B Equity			6,185,567	$3,000	$345
	Medical Devices & Equipment	Preferred Series C Equity			1,927,309	655	100
	Medical Devices & Equipment	Preferred Series D Equity			55,103,923	5,257	3,193
	Medical Devices & Equipment	Preferred Series E Equity			31,199,131	2,609	2,618
	Medical Devices & Equipment	Preferred Series E Warrants			10,535,275	1,252	271
Total Optiscan BioMedical, Corp.						12,773	6,527
Solar Spectrum Holdings LLC (p.k.a. Sungevity, Inc.)	Sustainable and Renewable Technology	Senior Secured Debt	August 2019	Interest rate PRIME + 8.70% or Floor rate of 12.95%, 4.50% Exit Fee	$12,000	11,770	11,683
	Sustainable and Renewable Technology	Common Stock			288	61,502	12,315
Total Solar Spectrum Holdings LLC (p.k.a. Sungevity, Inc.)						$73,272	$23,998
Stion Corporation	Sustainable and Renewable Technology	Preferred Series Seed Warrants			2,154	1,378	—
Total Affiliate Investments (3.68%)*						$87,423	$30,525
Total Control and Affiliate Investments (10.25%)*						$148,414	$84,938

* Value as a percent of net assets

(1) Stock and warrants are generally non-income producing and restricted.

(2) All of the Company’s control and affiliate investments are Level 3 investments valued using significant unobservable inputs.

SIGNATURES

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

	HERCULES CAPITAL, INC. (Registrant)
Dated: May 3, 2018	/S/ MANUEL A. HENRIQUEZ Manuel A. Henriquez Chairman, President, and Chief Executive Officer
Dated: May 3, 2018	/S/ GERARD R. WALDT, JR. Gerard R. Waldt, Jr. Interim Chief Accounting Officer