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G-III Apparel Group Ltd. (GIII)

Q1 2023 Earnings Call

CORPORATE PARTICIPANTS

Neal S. Nackman
Chief Financial Officer & Treasurer, G-III Apparel Group Ltd.

Morris Goldfarb
Chairman & Chief Executive Officer, G-III Apparel Group Ltd.

OTHER PARTICIPANTS

Alec Legg
Analyst, B. Riley Securities, Inc.

Dana Lauren Telsey
Analyst, Telsey Advisory Group LLC

MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by and welcome to the G-III Apparel Group First Quarter Fiscal 2023 Earnings Call. At this time, all participants are in a listen-only mode. After the speaker's presentation, there will be a question-and-answer session. [Operator Instructions]

I would now like to turn the call over to your host Neal Nackman, the company's, CFO. You may begin.

Neal S. Nackman

Chief Financial Officer & Treasurer, G-III Apparel Group Ltd.

Good morning and thank you for joining us. Before we begin, I would like to remind participants that certain statements made on today's call and in the Q&A session may constitute forward-looking statements within the meaning of the federal securities laws. Forward-looking statements are not guarantees, and actual results may differ materially from those expressed or implied in forward-looking statements. Important factors that could cause actual results of operations or the financial condition of the company to differ are discussed in the documents filed by the company with the SEC. The company undertakes no duty to update any forward-looking statements.

In addition, during the call, we will refer to non-GAAP net income, non-GAAP net income per diluted share and adjusted EBITDA which are all non-GAAP financial measures. We have provided reconciliations of these non-GAAP financial measures to GAAP measures in our press release, which is also available on our website. Also disclosed in our press release for your reference are last year's GAAP to non-GAAP results by quarter.

I will now turn the call over to our Chairman and Chief Executive Officer, Morris Goldfarb.

Morris Goldfarb

Chairman & Chief Executive Officer, G-III Apparel Group Ltd.

Good morning and thank you for joining us. Also joining me today is Neal Nackman, our Chief Financial Officer. We entered the fiscal year with strong momentum that continued throughout the first quarter of fiscal 2023 and exceeded both our top and bottom line guidance. As people go back to work, resume socializing and life continues to return to normal, customers are shopping to refresh their wardrobes and demand for our product remains strong.

Our retail partners are seeing significant growth in sales of our power brands DKNY, Donna Karan, Calvin Klein, Tommy Hilfiger and Karl Lagerfeld Paris. Given the positioning of our brands and better department stores, our business is much less impacted by the recent inflationary pressures, in particular our status brands Vilebrequin and Karl Lagerfeld are even further insulated on pace with the overall luxury market.

G-III has been able to successfully navigate a continued globally challenged environment because of our experienced leadership and agile world-class teams, our dominance across a broad range of categories, our flexibility in creating product, and a well-developed supply chain infrastructure which is one of our competitive strengths. This strong foundation and our entrepreneurial culture has enabled us to quickly pivot resources to anticipate and deliver right merchandise and the right categories with the right price point at the right time.

We're confident in our business and future growth opportunities and are raising our outlook. Net sales for the first quarter were $689 million, an increase of 33% compared to last year's first quarter net sales of $520 million above our guidance by approximately 15%. Net sales were approximately 9% above pre-pandemic levels. Non-GAAP net income was $0.72 per diluted share compared to non-GAAP net income of $0.50 per share in the first quarter last year.

Now, I'll update you on progress for each of our key priorities to deliver continued long-term profitable growth. Our first priority is to drive our power brands across categories. This was another strong quarter for our wholesale business registering growth across the board that once again outpaced our expectations. At G-III, our team is agile, moves quickly and has the foresight to see where the market is going.

When the pandemic hit, we quickly focused on driving our casual divisions including jeans, athleisure, casual sportswear and footwear growing them significantly over pre-pandemic fiscal 2020 levels. These businesses continued to perform well with sales slightly up compared to last year. In anticipation of people resuming social activities, we've once again rebalanced our mix. With sales up overall across our divisions, we decreased penetration of casual pandemic categories and shifted our production into more polished products, including dresses and career wear. These post-pandemic categories are now seeing strong acceleration in sales up over 35% to last year with AURs increasing over 25%.

Additionally, we shifted our production calendars to bring in inventory earlier and are well positioned to capture this robust demand. Outerwear also performed well. The cold weather in the first quarter of this year fueled broad-based demand for our lighter seasonally functional collections. For the fall 2022 season, we're prepared with inventory, have strong orders and a high single-digit list in average AURs. This was a particularly good quarter for our growing handbag business for Calvin Klein, DKNY and Karl Lagerfeld Paris.

Our newly launched Karl Lagerfeld handbags have gained substantial scale and doubled in distribution from last year now available on approximately 450 doors in North America. We had strength in dressier footwear and fashion sneakers for DKNY and Karl Lagerfeld Paris which are driving increases in AURs. Our second priority is to expand our portfolio through ownership of brands and their licensing opportunities.

Last month, we announced the acquisition of Karl Lagerfeld, which is an exciting milestone as it furthers all our strategic priorities. Given our track record of launching and growing this and other brands in North America along with the brands globally recognized the significance, we're confident in its future success. Additionally, we have a seven-year working relationship with Pier Paolo Righi, the brand's CEO and his management team and feel good about their ability to continue to guide this business.

Our collective expertise will accelerate its growth. Importantly, a 100% ownership of Karl Lagerfeld furthers our geographic reach. In our licensing division, we've created a well-developed capability that is a significant profit driver. Licensing a broader range of categories also expands our customer base. With the addition of Karl Lagerfeld, we now expect to generate over $65 million in annual royalty income. Across our own brands, we work with some of the best partners in categories that include fragrance, eyewear, intimates, kids and home.

This past quarter, we renewed some of our top licenses for DKNY and lined up licenses for Sonia Rykiel in kids, shoes and jewelry. Our third priority is to maximize omni-channel opportunities and leverage data. About a year ago, we accelerated our investment in digital and created a cohesive omni-channel strategy centered around the customer. We have the right team in place with technology and performance marketing experts along with new data analysts who are driving our business and our focus on utilizing data to learn more about our customers is yielding results.

Compared to pre-pandemic levels, digital sales of our product for the quarter were up approximately 60%. In addition, to our own direct-to-consumer segment, we have a strong omni-channel business with our retail partners. Our brands hold a significant presence on their growing websites and occupy some of the most desirable real estate in their stores. We're capturing market share as consumers are increasingly returning to stores for categories such as dresses and career wear. Our ability to deliver across channels continues to elevate our position as a vendor of choice to our retail partners.

Additionally, we've made minority investments in two emerging digitally native companies. These strategic investments create an exciting mutually beneficial relationship. We will test and learn in this space by using their technological expertise. It also provides us with revenue growth opportunities through product development and providing them supply chain services. Another component of our omni-channel is our own DKNY and Karl Lagerfeld Paris retail operations. We had a rebound in traffic despite continued challenges in tourism. Some store sales were up 30% for DKNY and 50% for Karl Lagerfeld.

This year we will add seven new Karl Lagerfeld Paris locations and will close about the same number of underperforming DKNY stores. We're focused on further driving omni-channel growth by improving the customers experience both digitally and in our brick-and-mortar stores. Our digitally focused brand marketing campaigns for DKNY and Karl Lagerfeld Paris are delivering results. Both businesses are growing their communities of loyalists with a curated group of celebrities and social media influencers. We're increasing our investment in performance and data-driven marketing in addition to developing our CRM capabilities.

Karl Lagerfeld's [indiscernible] (00:12:02) marketing will focus on its collaboration with Cara Delevingne, this will be a global branding initiative launching first in New York for fashion week followed by Dubai and Milan and wrapping up in Paris. Marketing investments in our own brands have contributed to building significant businesses as well as a wider consumer awareness and great brand equity. Our fourth priority is to extend our reach by developing our European based brand portfolio.

The Karl Lagerfeld acquisition significantly furthers our progress in this area together with the opportunities ahead for Vilebrequin, Sonia Rykiel and DKNY. We're developing our infrastructure, leveraging our leadership talent and creating synergies to build the solid foundation that will fuel these businesses. Additionally, Vilebrequin had a good quarter. Direct-to-consumer sales were up strong double digits compared to pre-pandemic levels and wholesale nearly doubled. We're expanding the brand's presence by adding approximately 10 company-owned and partner operated stores in Europe and in North America. We have a very strong lineup of collaborations coming for the year.

To further amplify the brand's visibility, we're in the process of acquiring and launching our first ever Vilebrequin beach club located in a prestigious vacation destination in the south of France. This will create an immersive customer experience and provide a differentiated marketing opportunity, which lends itself to franchising the concept. Looking ahead, we're expecting Vilebrequin to have a solid year.

As of 2021, recycled or recyclable materials represented 50% of the brand's collections and by 2023, we expect that figure to rise to 80%. Last year, the business launched Foundation Vilebrequin with a focus on protecting marine biodiversity, educating children on their environmental legacy and advocating for a more conscious fashion industry. This coincides with the progress we've made on our overall G-III corporate social responsibility initiatives last year.

Of note, we furthered our commitment to diversity, equity and inclusion. We're a founding member of the groundbreaking Social Justice Center at the Fashion Institute of Technology, a program that will increase opportunities for minorities coming into our industry. We also continued our partnership with the UNCF by fully funding 10 scholarships. Both initiatives include opportunities for students to gain first-hand experience here at G-III. Our 2022 CSR letters that will be posted and I encourage you to look at for more details on our efforts, it will be posted shortly.

In conclusion, we delivered better-than-expected top and bottom line results, a solid start of the fiscal year despite a challenging operating environment. Accordingly, we're raising our fourth fiscal year 2023 guidance. We now expect net sales to be approximately $3.24 billion and non-GAAP net income per diluted share to be between $4.40 and $5.50. This guidance is inclusive of approximately $140 million in net sales and approximately $0.10 per diluted shares for our newly acquired Karl Lagerfeld brand.

With a return to normal life, we remain optimistic about our business and ability to gain market share. I'll now pass the call to Neal for a discussion of our first quarter financial results as well as guidance for our second quarter and full year fiscal 2023.

Neal S. Nackman

Chief Financial Officer & Treasurer, G-III Apparel Group Ltd.

Thank you, Morris. Our first quarter results exceeded our guidance. Net sales for the first quarter ended April 30, 2022 increased approximately 33% to $689 million from $520 million in the same period last year. Net sales of our wholesale operations segment increased approximately 33% to $681 million from $512 million last year and were up 19% compared to pre-pandemic net sales of $571 million in the first quarter of fiscal year 2020.

Net sales of our retail operations segment were $28 million for the first quarter up 44% compared to net sales of $19 million in last year's first quarter.

Our gross margin percentage was 35.7% in the first quarter of fiscal 2023 compared to 37.6% in the previous year's first quarter. The gross margin percentage in the first quarter was expected to be lower in the same period last year due to the inflationary increases in our costs including increases in freight expense.

Cost increases were partially offset by price increases implemented by us and improvements in the promotional environment. Wholesale operations segment gross margin percentage was 34.1% compared to 36.3% in last year's comparable quarter. The gross margin percentage in our retail operations segment was 50% compared to 50.3% in the prior year's quarter.

SG&A expenses were $185 million in this quarter compared to $142 million in last year's first quarter and $202 million in the pre-COVID first quarter of fiscal 2020.

The current quarter's SG&A as a percentage of sales was 26.9% compared to 27.2% in the first quarter of last year and 31.9% in the pre-COVID first quarter.

We had larger than usual other expenses. This is mainly attributable to foreign currency translation losses primarily associated with the strength of the dollar. Large portion of these charges are associated with the Karl Lagerfeld acquisition as we accumulated euro-based funds in anticipation of the closing of the transaction.

These charges are one-time in nature and accordingly we are providing non-GAAP results this quarter to adjust for these charges for expenses related to the Karl Lagerfeld transaction and for non-cash imputed interest expense.

We expect to continue including non-GAAP results in our quarterly earnings releases for the rest of this year.

Net income for the quarter was $30.6 million or $0.62 per diluted share compared to $26.3 million or $0.53 per diluted share in last year's first quarter. Net income for the pre-pandemic first quarter of fiscal 2020 was $12 million or $0.24 per diluted share and included direct losses from Wilsons and Bass store operations of $6 million or $0.11 per share.

Non-GAAP net income per diluted share was $0.72 per diluted share compared to $0.56 per diluted share in last year's first quarter. Our inventory levels are up approximately 59% compared to last year as we have pulled up our production calendar in anticipation of supply chain challenges.

This increase is predominantly driven by in-transit inventory, that makes up approximately 60% of that increase. Last year's inventory levels were unusually low. As compared to pre-COVID wholesale inventory levels in the first quarter of fiscal 2020, we are up 26%.

Considering the pull up of our production calendar, we feel very good about our inventory position and its composition.

We ended the quarter in a lower net debt position of $83 million compared to $118 million in the prior year. We had cash and availability under our credit agreement of over $1 billion at the close of the quarter. We believe that our liquidity and financial position provided some flexibility to take advantage of acquisition opportunities and invest in our future growth.

Subsequent to the quarter end, we funded our recently closed Karl Lagerfeld transaction with approximately $214 million of cash on hand.

As for our guidance, as Morris indicated based on the strong demand for our product and our order book we feel good about our business giving us the confidence to raise our outlook for the year. Our raised guidance for fiscal year 2023 contemplates current lockdowns in China, expected increased shipping costs and delays in receipt of goods.

The guidance does not contemplate any impact from additional COVID-19 variants, significant worsening in global inflation rates or consumer sentiment.

For fiscal 2023, our guidance now includes the expected results for the newly acquired portion of the Karl Lagerfeld brand. We expect net sales to be approximately $3.24 billion and non-GAAP net income of between $213 million and $223 million or between $4.40 and $4.50 per diluted share. This is inclusive of approximately $140 million in net sales and approximately $0.10 in net income per diluted share to the acquired Karl Lagerfeld brand.

This guidance compares to net sales of $2.77 billion and non-GAAP net income of $208 million or $4.20 per diluted share for fiscal year 2022. Full year fiscal 2023 adjusted EBITDA is expected to be between $360 million and $370 million compared to adjusted EBITDA of $350 million in fiscal 2022.

For the second quarter of fiscal year 2023, we expect net sales of approximately $600 million compared to $483 million in the same period of the previous year.

Non-GAAP net income for the second quarter of fiscal 2023 is expected to be between $21 million and $26 million or between $0.45 and $0.55 per diluted share. This guidance compares to non-GAAP net income of $20 million or $0.41 per diluted share for fiscal 2022.

Let me add some context to our modeling or the line items. The inclusion of the acquired Karl Lagerfeld results is expected to increase our gross margin and SG&A percentages as this business has a higher direct-to-consumer penetration, which generally has higher gross margins and also a higher SG&A cost base.

Accordingly, we now expect full fiscal 2023 gross margins to be up for last year's gross margins and SG&A to delever. Our second quarter will be less impacted from the acquisition since the Karl Lagerfeld business will only be reflected by us for one month during that quarter. Similar to our first quarter and as we have previously stated, we do expect to have a lower gross margin percentage for the second quarter compared to the prior year and a flattish SG&A percentage as compared to the prior year's quarter.

Then as we anniversary the increases in freight, and inflationary pressures, in the back half of last year we expect gross margins in fiscal year 2023 to be higher than fiscal 2022.

We have estimated tax rate of 26% for the balance of the year. That concludes my comments, I will now turn the call back to Morris for closing remarks.

Morris Goldfarb

Chairman & Chief Executive Officer, G-III Apparel Group Ltd.

Thank you, Neal and thank you all for joining us today. I have a minor correction, I believe that I stated that our net income per diluted share will be $4.40 to $5.50, actually it will be $4.40 to $4.50. Forgive me for the typo.

G-III has a culture of entrepreneurship, agility and flexibility with a track record of navigating through tough environments. We remain extremely focused on our strategic priorities to deliver continued long-term profitable growth, which includes driving our power brands across categories, further expanding our portfolio through ownership of brands and their licensing opportunities, extending our reach by developing our European-based brand portfolio, maximizing digital opportunities and use of data and finally continuing to innovate to stay relevant.

We're optimistic about the year and continue to believe there is tremendous opportunity to unlock the potential of our globally recognized brands and grow our business.

I'd like to thank our entire G-III organization and all of our stakeholders for their continued support. Operator, we're now ready to take some questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question comes from Susan Anderson with B. Riley.

Alec Legg
Analyst, B. Riley Securities, Inc.
Q

Hi, good morning Alec Legg on for Susan and nice job on the quarter and can you talk about the Karl Lagerfeld brand more in detail? What percentage historically has been wholesale versus digital or direct-to-consumer? And then what's the operating margin profile of that brand versus the rest of the enterprise?

Neal S. Nackman
Chief Financial Officer & Treasurer, G-III Apparel Group Ltd.
A

Yeah, with respect to the numbers the operating margin that we're anticipating this year is mid single digits. Ultimately, we think that this brand similar to the ownership and the brand we got with DKNY will actually be a mid single-digit, a mid double-digit operating margin. Again no royalties, there is a good licensing revenue stream to the business and those help enhance operating margin percentages.

In terms of the mix between direct-to-consumer, it is more direct-to-consumer probably about 60% if you look at the [indiscernible] (00:27:26) and digital penetrations. I would also point out that even with respect to the wholesale business again not paying a royalty the margins on that business are also higher than what we generally experience across our wholesale segment today.

Morris Goldfarb
Chairman & Chief Executive Officer, G-III Apparel Group Ltd.
A

So, what we also have is as a license when we operated Karl Lagerfeld Paris, our distribution was limited to North America. Now that the boundaries are down, the borders are down and Karl Lagerfeld Paris will be distributed throughout the world and Karl Lagerfeld which is the Halo brand will be distributed much more aggressively in North America. So, we're going to benefit from some tremendous synergies in building this business for the future.

Alec Legg
Analyst, B. Riley Securities, Inc.
Q

Fantastic and then just a follow-up on inventory levels. I know it's up nearly 60% year-over-year but if you look at say versus 2019 it's still pretty lean because now you don't have the G.H. Bass and Wilsons stores. I guess are there any categories which you have more of and do you think the supply chain pressures and the timeline is easing?

Morris Goldfarb
Chairman & Chief Executive Officer, G-III Apparel Group Ltd.

A

So our inventories are well balanced as I discussed earlier in our presentation. We pivoted as we saw our casual wear and pandemic apparel slowdown. We modified our inventory mix and brought back the more polished in career wear balance to what it needed to be.

So, our inventories are in good shape as far as maybe what I would like a little bit more of career wear is in high demand and we're in short supply that we're correcting that and our dress inventory could be at a higher level. So, I think we're well balanced for the future, our [indiscernible] (00:29:33) inventory is coming in earlier than ever. We wanted to get out of the way of supply chain issues both delays at the port and container delays. So, we took that opportunity and brought our -- some of our containers in earlier. There is a tremendous amount -- half of our inventory, still resides at the ports, it's not all being cleared, it's not as if it's been sitting in the warehouse for a long time, most of – a good deal of it is still not in the warehouse and our order book is up significantly.

Alec Legg
Analyst, B. Riley Securities, Inc.

Q

Fantastic. Hopefully, the inventory can make its way to the consumer soon and best of luck for the rest of the year.

Morris Goldfarb
Chairman & Chief Executive Officer, G-III Apparel Group Ltd.

A

Thank you, very much. Thanks for your questions.

Operator: The next question comes from Jay Sole with UBS.

Q

Hi, good morning. This is [indiscernible] (00:30:27) on behalf of Jay Sole, thanks for taking our question. I wanted to ask about the gross margin. I believe you mentioned you expected to be higher for the full fiscal year. So I was wondering if you could elaborate a little bit more on the puts and takes and how should we think about that trajectory for Q2 and the rest of the quarters? And then maybe if you could comment a little bit about the performance in Tommy Hilfiger and Calvin Klein, how have these brands performed with whole shift also more towards [ph] dress in fashion in a way from (00:31:05) casual? Thank you.

Neal S. Nackman
Chief Financial Officer & Treasurer, G-III Apparel Group Ltd.

A

Sure, as we've been saying this is a year of much higher inflationary pressures that includes the freight category. We started to see those hit us last year towards the end of the year. So when we anniversary the back half of that, we will have that a little bit in the rearview mirror. We have lifted prices, we selectively lifted prices last year. It's been more robust in terms of the price lift that we've done this year to offset those increases and while we do see so many pressure in general on gross margins as a result of those cost inputs. We think we're managing through that process very well.

Morris Goldfarb
Chairman & Chief Executive Officer, G-III Apparel Group Ltd.

A

As it relates to both Tommy and Calvin Klein, I think you know we produce most of the woman's apparel for both brands and we're limited to distribution in North America and our business is quite good. Both brands are performing very well. There is high demand for pretty much in all category, there is a little bit of a slowdown in the casual side of it but the polished part of the business is exceptionally good. No slowdown in Tommy and Calvin Klein at all, those are great brands for us. Thank you, [indiscernible] (00:32:31), thanks for your question.

Q

Thank you.

Operator: Our next question comes from Dana Telsey with Telsey Advisory Group.

Dana Lauren Telsey
Analyst, Telsey Advisory Group LLC

Q

Hi, everyone and nice to see the progress. As you think about the order book going into the fourth quarter and just the balance of the year, what are you seeing, is it different in terms of how department stores are ordering or what they are ordering for the balance of the year? And then Morris, any perspective on international versus domestic reach of the brands and how they are progressing? Thank you.

Morris Goldfarb
Chairman & Chief Executive Officer, G-III Apparel Group Ltd.

A

Thank you, Dana. Department stores are managing their inventory differently than the past. The margins that they are working with are significantly better and their focus is turn on inventory versus a surplus of inventory. There is a benefit to all of that, there are less promotions, promotions are done, product is put on sale not nearly as often as pre-pandemic era and we're accommodating the needs of the department store where brick-and-mortar is picked up and digital business has slowed down a little bit. But the balance is good and the profile of how the product is merchandised and less promotions leave us comfortable that we are able to raise our prices to accommodate a little bit of what we're going through on inflation and it's proving out, our average unit retails are up and strategy is not a bad one for us.

As it relates to international, we don't have distribution as I said earlier for our Calvin Klein or Tommy Hilfiger internationally, but we finally have a strong platform of our own brands that are distributable throughout the world and we are now with the acquisition of Karl Lagerfeld have a significant platform that will achieve scale over time. Vilebrequin is very special, it's a high-end, it's probably the most status swimwear brand, men swimwear brand in the world and that has got limited distribution, it's in every high-end resort in the world doing well margins are exceptionally well. We've got great plans for that in the future internationally.

And Lagerfeld as I said this acquisition gives us great exposure with both the premium brand as well as the diffusion piece which is Karl Lagerfeld Paris. There are stores that Karl Lagerfeld Paris might be better suited for in Europe and we're seeing great opportunities with that, not to leave out DKNY, we're creating a major footprint with DKNY throughout the world. So G-III as a resource globally will be significant in the years to come, so thank you Dana. Thank you for your questions.

Dana Lauren Telsey
Analyst, Telsey Advisory Group LLC

Q

Thank you.

Operator: [Operator Instructions] Our next question is a follow-up question from Jay Sole with UBS.

Q

Hi, thanks for taking my question again. I just wanted to follow-up on Karl Lagerfeld acquisition, I think you mentioned earlier that you are anticipating this business to be in mid-single digit operating margin and then it could reach a mid double-digit operating margin, I mean I just wanted to ask what are you considering in terms of the timeframe for that in terms of like the outyears or what's the timeline that you are considering for the improvement in the margins in this business? Thank you.

Neal S. Nackman
Chief Financial Officer & Treasurer, G-III Apparel Group Ltd.

A

Yeah, look, I don't think that we want to be that specific on it, but we do expect these margins to improve quickly in the short term.

Q

Got it, thank you.

Morris Goldfarb
Chairman & Chief Executive Officer, G-III Apparel Group Ltd.

A

We're improving supply chain, the scale of the business has changed. There certainly will be improvements in margin and contrary to Neal I am going to take my chances and tell you that it's a short-term improvement -- short-term calendar, it'll improve very quickly.

Q

Got it, thank you very much.

Operator: And I'm not showing any further questions at this time. I would like to turn the call back over to our host for any closing remarks.

Morris Goldfarb
Chairman & Chief Executive Officer, G-III Apparel Group Ltd.

Thank you all. Thank you for your questions and your continued support. Thank you very much. Have a good day.

Operator: Ladies and gentlemen, that concludes today's presentation. You may now disconnect and have a wonderful day.