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G-III Apparel Group Ltd. (GIII)

Q3 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, and thank you for standing by. Welcome to the G-III Apparel Group Third Quarter Fiscal 2022 Earnings Call. At this time, all participants are in a listen-only mode. After the speakers' presentation, there will be a question-and-answer session. [Operator Instructions]

Please be advised that today's conference is being recorded.

I would now like to hand the conference over to your speaker today Neal Nachman, CFO. Please go ahead.

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.

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. I'm pleased to report that the momentum in the first half of the year continues into the second half. For our third quarter of fiscal 2022, we delivered outstanding results with both our top and bottom line, exceeding our guidance. Our world-class team continues to deliver the right product at the right time to meet significant consumer demand and, importantly, capture additional market share. We continue to maintain flexibility in navigating supply chain disruptions.

Given the significant demand we're seeing across our brands, combined with our strong order book, we have the confidence to raise our full year fiscal 2022 guidance. We now expect to deliver the highest annual net income per diluted share in our company's history, exceeding pre-pandemic fiscal 2020 results by approximately 26%. We expect to enter the new fiscal year in our strongest financial position, affording us the flexibility to invest in our future growth, and continue to elevate our position as a global leader in fashion.

Now, let's review the third quarter fiscal 2022 results. Net sales for the third quarter were ahead of our guidance at approximately $1.02 billion. This represented an increase of 23% compared to last year's third quarter net sales of $827 million. This increase in our third quarter net sales was driven by our wholesale segment where net sales for the quarter were $1.01 billion, up 29% compared to $783 million in last year's third quarter.

Importantly, third quarter net sales for our wholesale segment are quickly approaching pre-pandemic levels, down only 5% from third quarter net sales two years ago. Third quarter net income was $2.16 per diluted share which exceeded the midpoint of our guided range by 27%, and is our highest quarterly diluted net income per share in our history. This compares to a net income of $1.29 per diluted share in the third quarter last year and net income of $1.97 per diluted share in the third quarter two years ago.

Now, let's walk you through some of our third quarter highlights. Our inventory levels are in good position and we continue to experience strong selling at retail across the full range of our casual offerings including outerwear, athleisure, sportswear, jeans, as well as dresses, and career wear. Customer response to our fall fashion collections has been strong and we're well-positioned for the holiday season with gifting programs.

With robust momentum in each of these categories, we believe our business will continue to grow and we have opportunity for market share gains across these businesses.

Outerwear is a key business for us, and in the third quarter as we expected, it performed well with three leading categories: comfort casual product that supports an active lifestyle; transitional, or layering pieces; and an assortment of soft shell jackets.

In athleisure and casual sportswear, we focused on a cleaner aesthetic, new fits and a collection of key layering pieces to transition into colder weather. Comfort, performance, and functionality drive the athleisure business while polished pieces anchor the casual sportswear business.

Jeans across our power brands again exceeded our expectations and have become a significant contributor to our overall results. Along with denim bottoms, these collections offer a broad assortment of tops, soft shirts, sweaters, blazers and casual dresses that have become an important wardrobe builder for a younger customer to build a complete outfit.

Our DKNY and Karl Lagerfeld Paris footwear business far exceeded our expectations with net sales, almost 50% higher than pre-pandemic levels. Handbags for DKNY, Calvin Klein, and Karl Lagerfeld Paris also outperformed, and are approaching pre-pandemic levels with AURs in both categories up solid double digits.

The demand that began in the second quarter for our dresses and career wear accelerated, and sales at retail surpassed pre-pandemic levels with strong sell-throughs. Karl Lagerfeld Paris, this business is outpacing our expectations. Pre-pandemic, the brand's total net sales were $135 million, and this year the total sales footprint is to be approximately $175 million.

Last year, we launched Lord & Taylor, one of the brand's largest customers, but we were able to expand the collection at Macy's which has been incredibly successful and rapidly growing. We're also adding ten retail stores this year. We believe Karl Lagerfeld Paris is on a clear path to achieving annual net sales of $500 million over the next several years.

Digital remains a key priority. We're investing to capture and accelerate growth to become a best-in-class omni-channel organization. Compared to two years ago, sales on our partner sites increased over 45%, and over 60% on our own sites.

In China, digital sales are now larger than store sales, and Vilebrequin's digital sales were also up compared to two years ago. We remain focused on several digital priorities. Improvements to our digital platforms for DKNY and Karl Lagerfeld Paris are progressing well. With the first phase complete, the new look and feel of the sites has a modern aesthetic that customers are responding to.

In the next phase, our replatforming will add additional enhancements to technical operations to allow seamless navigation of these sites. This is expected to boost performance and productivity next year. We continue to invest in improving our technological and operational capabilities with data analytics, best-in-class reporting tools, and building our internal team.

We're creating operational efficiencies that standardize the workflow across our brands to become more agile, efficient, and effective. We're also building out our capabilities to grow our presence on leading pure-play global retail sites including Amazon, Zalando, and Fanatics. These investments are already providing internal and external insights into customer behavior, and are actionable and are increasing our ability to make better, faster data-driven decisions. Our direct-to-consumer warehousing and shipping is transitioning to our new logistics partner, GEODIS, which will drive operational efficiencies.

In marketing, we're increasing our investments with the focus on digital to drive qualified new and younger audience to our brands through a combination of paid media, celebrity seeding, and influencer marketing. DKNY's campaign features diverse and relatable influencers, and the Karl Lagerfeld Paris campaign highlights our exciting new Après ski collection. Both are leveraging across our digital ecosystem with a multi-prong approach that is building momentum into the holiday season.

Our international business for DKNY is growing. We're thoughtfully expanding our omni-channel footprint with wholesale partner operated stores and territories in addition to pure-play sites. In Europe, sales are back to pre-pandemic levels even with restrictions in place. We entered Turkey and Israel through a wholesale distribution, and will open two new partner operated stores for Donna Karan this quarter, one in Saudi Arabia, one in Riyadh, with the third to follow next year in Kuwait.

In China, we expect to double our sales this year as compared to two years ago. Vilebrequin registered another strong quarter with positive retail sales growth compared to pre-pandemic levels, and double-digit growth in the US. We celebrated the 50th anniversary of the brand with exclusive collaborations including Palm Angels and Space Jam, the movie, creating increased customer interest. This status brand expanded offering across lifestyle and athleisure categories, are driving sales especially in warm weather destinations which are becoming primary residences.

The wholesale order book including distributors operating Vilebrequin stores is strong, setting the stage for accelerated growth into next year. We believe there continues to be a meaningful opportunity to expand the brand. Licensing our own brands enables us to grow into additional lifestyle categories and international markets. This generates a capital-light royalty stream that is highly accretive and an important profit driver.

We've created solid licensing royalty income based with best-in-class partners in categories like fragrance, kids, watches, intimates, and sleepwear. For DKNY and Donna Karan, we have approximately 25 licenses, and the brands' total sales at retail are approaching $2 billion. This quarter we announced that Inter Parfums will take over their fragrance license with much more ahead. We'll continue to leverage our expertise in these partnerships to expand our brands' presence across the portfolio.

Now, let's look at our retail operations. Trends continue to improve in-store, online, and through our virtual selling programs which we consider a third leg to our omni-channel operating model. As I mentioned on last quarter's call, we're opening some new stores with good economic terms. This quarter we opened four new Karl Lagerfeld Paris stores which are off to a great start. We expect to end the year with 36 DKNY and 23 Karl Lagerfeld Paris stores. As we thoughtfully expand the omni-channel footprint, we expect to be able to further leverage our expense base.

Now, let me discuss a few initiatives we're working on with significant potential ahead. We just completed the acquisition of Sonia Rykiel an iconic luxury European fashion brand with incredible global awareness. We're in the early stages of the relaunch which leverages the backend infrastructure of our European operations. Our first collections across multiple categories are expected to be available next fall in France, then rapidly expand throughout Europe, and then globally. We believe in the untapped potential for this brand.

Another initiative we've been working on leverages a brand we already own G.H. Bass. There is significant value in its 150-year-old rich legacy which provides a licensing royalty stream. Additionally, we're harnessing the brand to develop incremental businesses and just launched Bass outerwear – Outdoor. The collection capitalizes on a secular shift towards an active outdoor lifestyle by offering practical, innovative, and sensibly designed footwear, and apparel for men, and women. It launched this past quarter in 150 Macy's stores, on Macy's.com and [ph] bass.com (00:15:21) and is off to a good start.

With this launch combined with our Karl Lagerfeld Paris men's business, we're developing a men's apparel design and production capabilities which presents an additional growth avenue. Both Sonia Rykiel and Bass Outdoor represent untapped opportunities for growth in our wholesale business as we expand distribution for this brands.

Summing up the third quarter, based on the continued strength of our business, our flexibility to adjust as needed to capitalize on market share opportunities and incredibly strong order book, we're raising our guidance for the full 2022 fiscal year. We now anticipate full fiscal year net sales to be approximately $2.77 billion, wholesale net sales of fast approaching pre-pandemic levels of two years ago. We expect to deliver our highest annual net income per diluted share exceeding pre-pandemic results in fiscal 2020 by approximately 26%. We also expect to be in our strongest financial position.

I'll now pass the call to Neal for discussion of our third quarter financial results as well as the guidance of the full fiscal year 2022.

Neal S. Nackman

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

Thank you, Morris. Net sales for the third quarter ended October 31, 2021, increased approximately 23% to $1.02 billion from $827 million in the same period last year and were above our guidance of $1 billion. Net sales of our wholesale operations segment increased approximately 29% to $1.01 billion from $783 million last year. Net sales of our retail operations segment were $26 million for the third quarter compared to last year's net sales of $58 million. This decrease is a result of the restructuring of our retail segment in which all the Wilsons Leather and G.H. Bass store operations were closed by the end of fiscal 2021.

Sales at our DKNY and Karl Lagerfeld Paris businesses were up compared to the prior year when sales were impacted by the pandemic.

Our gross margin percentage was 34.2% in the third quarter of fiscal 2022 compared to 36% in last year's third quarter. Last year's gross margins included benefits from COVID-related adjustments. Our gross margins were 35.4% two years ago. The current year's decrease compared to two years ago is primarily attributable to the decreased penetration of the retail segment due to the store closures.

Wholesale operations segment gross margin percentage was 33% compared to 35.5% in last year's comparable quarter and 33.2% in the comparable quarter two years ago. Wholesale gross margin percentages in this year benefited from clean inventories at retail, resulting in less promotional activity, combined with selective price increases. These improvements were offset by the significant increase in freight cost which we had anticipated would have more of an impact on gross margins in the second half of the year. Last year's gross margins included significant one-time benefits from the reversal of previously anticipated markdown accruals that were no longer necessary due to the reduction in sales to our retail customers.

The gross margin percentage in our retail operations segment was 49.8% compared to 33.9% in the prior year's quarter and 49.3% two years ago. Last year's percentage was negatively impacted by the restructuring of our retail operations segment which resulted in the liquidation of inventory in connection with closing stores.

SG&A expenses were $182 million in this quarter compared to $178 million in last year's third quarter. The increase in expenses compared to last year is correlated to an increase in sales as well as an increase in compensation expense, primarily as a result of bonus accruals offset by reduction in our retail store expenses and bad debt expenses.

Net income for the third quarter was $107 million or $2.16 per diluted share compared to $63 million or $1.29 per diluted share in last year's third quarter and included direct losses from Wilsons and Bass store operations was $12 million or $0.25 per share. Net income for the third quarter two years ago was $95 million or $1.97 per share and included direct losses from Wilsons and Bass store operations of $4 million or $0.08 per share.

Looking at our balance sheet accounts receivable were $844 million compared to $721 million at the end of the third quarter of the previous year. Inventory decreased to $449 million from $462 million at the end of the third quarter of last year.

We ended the quarter in an improved net debt position of $238 million compared to $359 million in the prior year. We have cash and availability under our credit agreement of over $900 million. We believe that our liquidity and financial position provide us the flexibility to invest in our future growth and continue to elevate our position as a global leader in fashion.

As per our guidance, as Morris indicated, based on strong demand for our product and our order book, we feel good about our business giving us the confidence to raise our previously provided guidance. Our guidance does not include the impact of the current supply chain conditions – does include the impact of the current supply chain conditions and delays in receipts. However, our guidance does not contemplate any pandemic-related impacts that we're not aware of already. We have not anticipated new store closures or the impact of tighter government restrictions that could arise from the recent variant or other new variants.

For the full fiscal year ending January 31, 2022, we now expect net sales of approximately $2.77 billion compared to $2.06 billion last year. Adjusting for the closed Wilsons Leather and G.H. Bass store sales of $252 million in fiscal 2020, the current guidance leaves us approximately 5% below our pre-pandemic sales levels in fiscal 2020. We now expect net income for the full fiscal year 2022 to be between $180 million and $190 million or between $3.65 and $3.75 per diluted share. This will be the highest annual net income per diluted share in our company's history, exceeding pre-pandemic fiscal 2022 results by approximately 26%.

This compares to net income of $24 million or $0.48 per diluted share in fiscal year 2021 and $144 million or $2.94 per diluted share in fiscal 2020. For your reference, disclosed in our press release issued this morning is the impact by quarter for the last two fiscal years of the Wilsons Leather and G.H. Bass store operations.

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. G-III has emerged as an even stronger organization by successfully navigating the pandemic. Our high-performing and forward-thinking teams combined with our experienced senior leadership have consistently executed through challenging environments and delivered great results to our stakeholders.

We will remain disciplined in our approach with a keen eye on fueling profitable growth. With our globally recognized power brands and our dominance in the diversified range of lifestyle categories, G-III remains a vendor of choice in our industry. Given the strong demand we're seeing across our brands, combined with a strong order book, we're confident in our business outlook for the remainder of the year.

We have the ability to use our balance sheet, talent expertise and capabilities to further expand our global reach and are well-positioned to gain market share over time and increase shareholder value. I'd like to thank our entire G-III organization and all our stakeholders for their continued support.

Operator, we're now ready to take some questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from Ed Yruma with KeyBanc. Your line is open.

Edward Yruma
Analyst, KeyBanc Capital Markets, Inc.

Q

Hey, good morning guys. Morris, congratulations on the fantastic quarter. I guess just a couple of questions for me. First, obviously very strong margin performance. How much of this is due to just kind of lower kind of markdowns, lower concessions versus what's more pricing? And I guess I'm just trying to understand kind of what's transitory given the industry inventory condition versus what you think some more permanent step-up in margins.

And then as a follow-up you guys have some very constructive comments on Lagerfeld at Macy's. I guess how is the business size wise relative to when it was at Lord & Taylor and how should we think about that ramp to $500 million? Thank you.

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

A

Thank you, Ed. Thank you for your questions. Our margin enhancements are partly due to how well we buy. We were fortunate enough to be on target, and our choices of categories to go after with the experience, the knowledge and I would say maybe gut feeling that categories that were not in favor at the breakout of the pandemic that would likely come back.

We negotiated all our purchases. We brought down our initial pricing and own the inventory in anticipation of new good business coming across. With that, our retailers found that they could increase the price points, the average unit retails on our primary categories. They prospered as well as we did. So, the margins are likely to continue. We've proven out important price points that elevate the average unit retail and support our initiatives of going out and buying fairly aggressively for the coming year.

Our order book supports good business going forward. Our breadth of distribution, and now as the further penetration of the globe, historically we've been a North American resource, pricing is also enhanced by our distribution in Europe and in China as well as the Middle East. So, we're comfortable with our pricing.

The Lord & Taylor business, when we acquired our interest in Karl Lagerfeld, the intention was to build Lord & Taylor, Dillard's, Nordstrom's and maybe Bloomingdale's business and The Bay in Canada. What afforded us that opportunity was the exit of Jones New York from our industry. We took the real estate that historically has been some of the best real estate at retail and filled it with Karl Lagerfeld Paris product in the accounts that I mentioned.

Performance was good. Lord & Taylor was the best of the group; and unfortunately, Lord & Taylor went into bankruptcy. We felt that we had sufficient opportunities with Lord & Taylor, The Bay, Dillard's that we would leave Macy's for a later date. That date came sooner than expected and Macy's has been a great supporter of all our initiatives. And in Macy's true form, they give us 75 doors to open with. We're headed towards 200 doors and likely to finish the year with 250 to 300 doors of Karl Lagerfeld Paris and the initial performance has been great.

We've gotten better on the product side. We're dead on target as to what the DNA of the brand should be and the sell-throughs at every retailer are just amazingly strong. So, we feel comfortable that within next few years $500 million in top line sales is not a problem to achieve.

Edward Yruma
Analyst, KeyBanc Capital Markets, Inc.

Q

Great. Thanks so much.

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

A

Thank you, Ed. Thanks for your question.

Operator: Thank you. Our next question comes from Erinn Murphy with Piper Sandler. Your line is open.

Erinn E. Murphy
Analyst, Piper Sandler & Co.

Q

Great. Thank you. Good morning, and happy holidays. A couple of questions maybe Morris, first for you. You have always been very nimble on the supply chain side. I'd like to hear a little bit more about your ability to get products to market in a timely manner. It sounds like there is a little bit of built-in higher freight cost. And then what's the balance of air freight versus ocean right now and how prolonged do you see in your crystal ball, of course, these challenges persisting through into 2022 ? And then I have follow-up.

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

A

Let me start with your last question first. We believe that we'll incur transportation issues pretty much through all of 2022. The steeper or the more aggressive problems will probably hit us for Q1 and Q2, and then calm down for the back end of the year. That's our anticipation. But as you being part of our shareholder group and our stakeholder group, you're clearly aware that sourcing is our core competency. We have a well-defined organization overseas. We have consistent suppliers. We were adamant that we were not going to leave relationships that we've had for 30 and 40 years and traveling to countries that would present short-term growth problems.

So we maintained presence in our old friend's facilities and tell you the truth, that's really what saved us this year. The loyalty went both ways. We were loyal to them at the breakout of the pandemic and the payback was we got receipts of product that we bought in fairly reasonable time period. Most recently more affected by container space and container cost than adverse factory conditions.

So, we're comfortable again. We bought a fair share of product for 2022 receipts. We believe that we'll start to receive goods a little bit earlier than historic and that's our hedge. We have the capital to receive it. We have the warehousing to hold it and we have retailer cooperation to take in inventory and help facilitate our process. So, we're comfortable. I wish I could give you 100% comfort, I can't. These are strange times. But we believe we're in control of the bulk of our business.

In response to your question on what percentage air freight it's a small percentage of air freight. I don't have the number in front of me but, I would tell you it probably doesn't pass 5% of our receipts. We're predominantly floating all our product, we're capitalized to the ports that we receive in. We're offering a little bit of that and we're negotiating prices that we can live with for the coming year on freight costs.

Erinn E. Murphy
Analyst, Piper Sandler & Co.

Q

Great. Thank you so much for that. And then just the second question is just on your outlook for the holiday season. How has it started, what's your expectations in these critical weeks between Thanksgiving and Christmas? Thanks so much.

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

A

So, as we anticipated our coat business broke wide open in the last couple of weeks. There was a little concern the weather was a little warm and as the weather broke our sales also came to fruition, our business has been excellent for both Cyber Monday and Black Friday.

Our increases were better than most as I do the comparison and read. We highlighted Karl Lagerfeld as a stellar performer. Cyber Monday we were up comp to 2019 numbers by 119%. DKNY didn't fare as good but, they were up mid-teens and Black Friday, again Karl Lagerfeld was up sensationally well. It more than doubled in business. And DKNY was closer to flat. Traffic was down north of 20% and my early reads were more like 23% internally. And in spite of that, we're closing more transactions, our average unit retail is up, our margins are up and we are in a good position going forward.

And as you've seen or as you've heard, we've revised our budget for the year. We anticipate strong sales and dramatic growth going forward.

Erinn E. Murphy
Analyst, Piper Sandler & Co.

Q

Thank you and just, I haven't heard you say anything about Calvin or Tommy yet. Just curious on performance there? Thanks so much.

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

A

Our performance there is quite good. And Tommy has been excellent. Calvin Klein has been very good. We dominate the dress area in Calvin Klein at the department store level and we've cited our dress business being excellent, Calvin Klein leads the charge followed by DKNY and Tommy Hilfiger and those brands are strong in every category. And so, there's no slowdown. Our margins are better on our company-owned brands but our business is quite good on all our power brands.

Erinn E. Murphy
Analyst, Piper Sandler & Co.

Q

Thank you so much. And all the best for the holiday season.

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

A

Thank you, Erinn. And same to you.

Operator: Thank you. Our next question comes from, Susan Anderson, with B. Riley. Your line is open.

Susan Anderson
Analyst, B. Riley FBR, Inc.

Q

Hi. Good morning. Nice job on the quarter. I was wondering if you could maybe talk about the economics of the remaining retail business now that it's just DKNY and Karl. And then also when you expect -- where do you expect that to go particularly as you open those more profitable stores that you talked about in Europe. Thanks.

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

A

So, number one, let me hit the last point first. The stores that I cited in the Middle East were distributor stores. They are not company-owned stores but, actually it's great. Their knowledge of the region hedges our bet in cooperating and supplying product to Saudi Arabia, Riyadh and we believe that – we believe those stores will be great at no expense to us and no risk to us. The risk is failure and we take that seriously. So, we've researched it and it's a great time to launch Donna Karan in those regions.

Our stores, as I said in our prepared script, where the real estate is being negotiated differently than when we had north of 300 stores. There are kickouts in the event of failure. The risk is nowhere near what we had historically. And for the first time in our business career, we have two amazing brands to build on. When we had 350 stores it was Wilsons which was a seasonal coat store, launched as a leather chain and as leather evaporated so did the prosperity of the Wilsons stores. And then we had Bass where we mismanaged the product side of Bass. Today, we have DKNY with amazing product, with broad appeal and watch out when the tourists comes back. It's geared towards just pretty much everybody. It's a well-recognized throughout the globe. And Karl Lagerfeld recognized even better.

So, we will not build 300 Karl Lagerfeld stores in the US but there is a possibility that we build 50 stores within the next 3 to 5 years. DKNY, a little different. DKNY being more price-sensitive and broader appeal to the American population does have the opportunity to grow to be north of 100 stores with G-III. But we're cautious, we have a different management team and we have different systems evaluating our performance and our needs. So, much more comfortable and much more careful on how we build retail.

Susan Anderson
Analyst, B. Riley FBR, Inc.

Q

Great. And if I could just add one follow-up on DKNY, now that we're looking past the pandemic a little bit and it's back in growth mode, I'm curious if you can give us an update on just the sales base there and where you expect that brand to grow to longer-term and how you're thinking about the op margin for the brand. Thanks.

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

A

So, our business in DKNY continues to grow. We are approximately $500 million in wholesale sales. We have a digital business that is growing. And as I stated before, our licenses or licensing partners all told, we believe we have approximately $2 billion in retail sales with this brand.

We have best-in-0class licensees, contractually bound to good period of time. And continue to get better at our product. Our handbag business has turned around, it's exceptionally good. Our footwear business is doing well. And we're one of the top 3 or 4 brands in the country on categories like dresses, ready to wear, even performances picked up its pace.

So, we see dramatic growth. There is no reason that DKNY in our hands alone can't reach $1 billion in sales I have said that – I've said it before. And I firmly believe that within the next few years we can get there and with believe it or not better margin and better product.

Susan Anderson
Analyst, B. Riley FBR, Inc.

Q

Great. Thanks so much. Good luck this holiday.

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

A

Thank you. Thank you, Susan. Happy holiday to you.

Susan Anderson
Analyst, B. Riley FBR, Inc.

Q

You, too.

Operator: Thank you. Our next question comes from Jay Sole with UBS. Your line is open.

Jay Sole
Analyst, UBS Securities LLC

Q

Great. Thank you so much. I want to follow up on a question about supply chain. You made some comments in your remarks about high level impact of supply chain challenges on margins in this quarter. But is it possible to give a little bit more color, maybe detail like how many basis points, like how should we think about the actual impact on gross margins from the challenges? And also what's implied in the guidance for 4Q? And then how do you see that headwind trending as you get into 1Q and 2Q based on what Morris said to an earlier question? Thank you.

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

A

Sure, Jay. Thank you. If you noticed, our margins on the wholesale business were north of 35% in the first two quarters. You can see we're down below that. That really was what we anticipated. Without quantifying the specific amount, it was quite significant the impact from the freight increases. And with respect to the fourth quarter, we again expected that that impact will be greater than what we've seen in the first half. So, we're still expecting that our gross margins at the wholesale segment will exceed where we were two years ago, but that will be with higher freight costs.

As Morris mentioned as far as going into next year, very hard to determine how that happens. We think that assuming a lot of people are working very hard to try to smooth, analyze different parts of the whole supply chain. We do expect that we'll still have higher freight cost in the first half of the year, and those should put a little pressure on us; however, we're really pricing all of our Spring line. I think one thing for us is, it's a little bit – some of this is a little more visible to us this year than what we saw last year, and we're really pricing – we're trying to price into our product all of our inflationary pressures including the impact of freight.

Jay Sole
Analyst, UBS Securities LLC

Q

Got it. Okay. Thank you so much.

Operator: Thank you. Our next question comes from Dana Telsey with Telsey Advisory Group. Your line is open.

Dana Lauren Telsey
Analyst, Telsey Advisory Group LLC

Q

Good morning, everyone, and congratulations on the nice progress. It seems like the wholesale channel has strengthened. Morris, given your touch points with wholesale, how do you see the wholesale distribution channel changing both in digital and physical, and what does it mean for each of your brands differently? Thank you.

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

A

Thank you, Dana. Thanks for your question. That's actually a really good question. But wholesale, the assumption unfortunately is that wholesale means brick-and-mortar. It really doesn't. We've changed. The industry has changed so much that we see retailers spinning off their digital sites because they're not getting any credit for being pure-play digital, so they're creating pure-play digital.

Saks would be a great example of that, and creating value out of what was just an underlying assumption that it was traditional old line brick-and-mortar. So, we're approaching not far from 50% digital as wholesale under the wholesale umbrella, and that continues to grow the numbers kind of staggering in growth as we all know. And brick-and-mortar is getting better as traffic, and the comfort of going out and shopping stores comes back to us.

The brick-and-mortar stores are likely to do far better. They're not dinosaurs in my world and they're not dormant in my world. If you look at some of the new concepts that are coming through. Even Macy's, they have a new concept which is smaller usually gotten to and shop. The investment is significant on Macy's part and the reports that comeback is that they're doing well.

So, I'd say there is a future to brick-and-mortar as standalone. And we create – over time if Saks is successful in creating a spinoff of their digital piece, we'll find that we've doubled our distribution, there'll be a greater focus and greater growth on a standalone digital business and the standalone retail business.

So, I think they affect all our brands in some form or another. We addressed – if you follow our company which I know you do, Dana, we're luxury, we're mass, we're mid-tier, we're team license, we're Europe, we're Southeast Asia, we're China. We're going to get that customer regardless of where she tries to hide. We're going to find it. And I said her the next approach to our business is, we're going to build a men's business and we don't get her, we're going to get him.

We're an agile company that knows its way around the consumer and I think we've proved that out this company I would like to remind people that we started out as the leather company that did one jacket, one color, four sizes that's all we did and we got here and there is a long distance to go. So, we'll find that customer regardless where that customer is shopping.

Dana Lauren Telsey
Analyst, Telsey Advisory Group LLC

Q

And then just one quick follow up.

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

A

Dana, sorry I got a little wordy on it but...

Dana Lauren Telsey
Analyst, Telsey Advisory Group LLC

Q

No worries.

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

A

Okay.

Dana Lauren Telsey
Analyst, Telsey Advisory Group LLC

Q

Just one quick follow-up, regarding the obviously a lot of change at PVH given new personal personnel coming in. How is that working with you and the timing of licensing renewals with them? Thank you.

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

A

So, we've renewed Tommy Hilfiger and there is some time left on Calvin Klein and I've no reason to believe that it doesn't get renewed. There is new management and different dynamics as we all know. But we're here as we were before, we perform exceptionally well and we've said in script several times with the time as the wholesaler's choice of where to do business we've proved that out and I have no reason to believe that PVH would change their posture in keeping us as a partner.

Dana Lauren Telsey
Analyst, Telsey Advisory Group LLC

Q

Thank you.

Operator: Thank you. Our last question comes from Steve Marotta with C.L. King & Associates. Your line is open.

Steven L. Marotta
Analyst, C.L. King & Associates, Inc.

Q

Good morning, Morris and Neal. Neal, I know that you're not providing guidance obviously for next year but maybe you can comment with the exception of elevated shipping cost in the first half, are there other puts and takes either in the first half of the year through the whole year that you're looking at that would be say runners up to the puts and takes associated with the shipping, thanks.

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

A

Yes Steve, we're not – it's early for next year and obviously there's lots of new uncertainties but what we've accomplished this past year with respect to the wholesale part of our business is truly astounding. We're getting higher operating margins on that business with less volume than we did two years ago. We've got significant increase in operating profit in our wholesale business.

As I mentioned earlier, we think that we'll be able to offset inflationary pressures including the freight with respect to our original – our opening pricing. As Morris mentioned, we've always been great at sourcing so we think that will be a solid strength for us.

I don't see at this point any really, unusual callouts for next year, it's a bit early. I can tell you our order book for the spring is very, very strong, so we're very encouraged with the start. And we really expect to continue building off of what's really been a phenomenal year for us and what we expect to be a phenomenal year for us.

Steven L. Marotta
Analyst, C.L. King & Associates, Inc.

Q

Neal, one just quick follow-up to that. You mentioned your order book for Spring is stronger and I'm sure you don't want to quantify it and understandably so -- if my memory serves me correct in previous conversations that we've had, you've mentioned given the supply chain constraints that we had moved into this current year that you are actually ordering overseas much, much earlier. Is that still the case for delivery in the Spring, in other words that is one pretty critical offset to what it continues to be supply chain scenarios.

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

A

Yes, Steve, that's been part of our mitigating processes, we've been to try to move up the calendar, get ahead of whatever we can.

Steven L. Marotta
Analyst, C.L. King & Associates, Inc.

Q

Very helpful. Thank you.

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

Thank you all. Thanks for listening to our call and for your interest in our company. I'd like to wish everyone a happy, healthy and safe holiday season and best wishes for a New Year. Thank you all.

Operator: This concludes today's conference call. Thank you for participating. You may now disconnect.