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G-III Apparel Group Ltd. (GIII)

Q1 2020 Earnings Call

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

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to the G-III Apparel Group First Quarter Fiscal 2020 Earnings Conference Call. My name is Sheryl, and I will be your operator for today's call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session. [Operator Instructions] Please note that this conference call is being recorded.

I will now turn the call over to Neal Nackman. Sir, you may begin.

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

Thank you. Good morning, and thanks 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 share, and to 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.

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. With me today are Sammy Aaron, our Vice Chairman and President; Wayne Miller, our Chief Operating Officer; Neal Nackman, our Chief Financial Officer; and Jeff Goldfarb, Executive Vice President.

We are pleased to have begun the year with a good first quarter. Our first quarter performance was anchored by our winning formula of leveraging our power brands through successful design, development and execution of great product that resonates with consumers. The strength of our business continues to be represented by our five global power brands: DKNY, Donna Karan, Calvin Klein, Tommy Hilfiger, and Karl Lagerfeld.

In North America, we've achieved the status as the supplier of choice to our retail partners in many major apparel categories, including outerwear, sportswear, dresses, suit separates and performance. We quickly have achieved great recognition for creating some of the best handbags and footwear in the marketplace.

We're also expanding our international presence, where we see a significant runway for future growth. Now that we've completed a full year of having our own DKNY and Donna Karan product in stores and with the solid performance of our remaining power brands, G-III remains well positioned for continued growth into the foreseeable future.

Before I review the results of our first quarter, I wanted to address the topic of tariffs. As you all know, the first level of tariffs at 10%, which for us primarily impacted the handbag business, was just increased to 25% as of export dates commencing with May 10. This business represented approximately 7% of our annual net sales for fiscal 2019.

We estimate that the incremental 15% increase in tariffs for the remainder of fiscal 2020 will increase our cost by approximately $6 million. We've included this increase into our reaffirmed guidance issued today. We've been seeking to diversify our sourcing networks by arranging to move some production out of China, and also succeeded in obtaining price concessions from our Chinese vendors. In addition, we've obtained price increases from some of our customers here in the U.S.

As for the proposal to increase tariffs on the remaining categories imported from China, we've had in-depth conversation with our vendors and our retailers, and although there'll likely be short-term disruption, all parties are willing to share in the increased cost. We've not quantified the impact of the potential near-term disruption on our results of operations should these increases come into effect.

We believe that our customer who is shopping in department stores is one who appreciates aspirational brands and is willing to pay more for our products. These price increases will be supported by the fact that we have the best global power brands, well designed product at the highest quality, better real estate positioning in the stores and are always priced better than our competition.

Looking ahead, we recognize the need to further reduce our production in China to a level where we can still maintain the consistent high quality and craftsmanship that we've developed with our vendors over the past 40 years.

Now, on a few financial highlights of our first quarter, our results were in line with our bottom-line expectation and were led by continued outperformance in our wholesale business, which more than offset the challenges in our own retail operations. First quarter net sales were up 4% to $634 million. Our first quarter wholesale net sales increased 8% to $571 million. Our first quarter non-GAAP net income per diluted share was $0.25, as compared to non-GAAP net income per diluted share of $0.22 in last year's first quarter.

Now, let's provide you some details on our results. In our own retail operations for Wilsons and Bass, we were disappointed with our results. Comparable store sales decreased by 23% for Wilsons and 11% for Bass. As we mentioned on our fourth quarter earnings call, we've so far eliminated approximately $5 million of annualized expenses and salaries, which better positions us to deliver on our goal of reducing our retail losses.

The merchant teams have created compelling product for the upcoming fall season. We're continuing to review every opportunity to accelerate our path to profitability, including continued store closures, accelerating convergence of Wilsons and Bass stores into DKNY and Karl Lagerfeld Paris stores, and implementing additional operating efficiencies.

Now, let's turn to our wholesale business. Our largest business, Calvin Klein, represented in excess of $1 billion of our net sales in fiscal 2019 and performed well in the first quarter of this year. Our Calvin Klein business is a dominant resource across the women's apparel market. Excluding the impact from sales to Bon-Ton, we were pleased to deliver another quarter of solid top-line growth, which was led by dresses, sportswear and suit separates.

Additionally, as you may have seen the announcement this past Monday, we're thrilled to extend our partnership with PVH with our new women's CK Jeans license. We have all read about the resurgence of denim and we believe we are well positioned to leverage our market expertise in women's apparel to tap into the momentum and build a substantial lifestyle jeans collection.

Our retail partners are quite excited about the initial products they've seen. I know it's early, but based on our past experience with significant product launches, this business has the potential to get to $250 million in annual sales over the next several years. We expect the full launch for spring 2020 and do not expect a material impact on our results in this fiscal year.

Our Tommy Hilfiger business remained quite strong during the first quarter, with greater than 50% year-over-year sales growth. The strength in the business was broad based and was led by sportswear, dresses and suit separates. The strength of the business showcases our continued strong execution and expertise in design, merchandising, sourcing and selling, combined with a compelling brand management and marketing by our partners at PVH.

We continue to expand the distribution and reach of our Tommy Hilfiger product. I'm also pleased to highlight that this spring we launched various Tommy Hilfiger categories into approximately 150 Dillard's doors. We've also expanded Tommy Hilfiger Sport into numerous specialty stores, including Urban Outfitters, JD Sport (sic) [JD Sports] and PacSun, with additional launches still to come. We remain very excited about the meaningful opportunities to grow this business over the next several years.

Our Karl Lagerfeld business did well in the quarter, and we continue to be excited by the success of this brand that we introduced to the North American market. Looking ahead, Carine Roitfeld, the former Editor in Chief of Vogue Paris, stylist, fashion director and entrepreneur who has had a long history of collaborating and influencing

Karl Lagerfeld himself, has been entrusted to lead the brand's global creative styling for the upcoming three seasons.

On June 20, our own Karl Lagerfeld company in addition to the fashion house of Chanel and Fendi will host a significant memorial celebration for Karl Lagerfeld at the Grand Palais in Paris. This event will pay tribute to Karl's legacy and his unprecedented creativity which expanded beyond fashion to include design, photography, publishing, illustration and architecture.

As I mentioned on our year-end earnings call, fiscal 2000 (sic) [fiscal 2019] was the first full year of our brand repositioning and distribution of G-III developed product for our own DKNY and Donna Karan brands. We've learned much about how we can continue to build this business going forward. At $400 million in annual net sales in fiscal 2019, this has quickly grown into a meaningful business and represents one of our biggest growth drivers. For the first quarter of this year, we've registered stellar double-digit growth with strength across all categories, led by sportswear, handbags and shoes.

On the DKNY marketing front, we continue to leverage the momentum of the 100% DKNY campaign. Our digital branding efforts and high-impact premium outdoor media placements are ongoing and not only performing well, but also exceeding benchmarks of success across media channels. Last week, we launched the DKNY Pride Capsule collection, playing off the 100% DKNY concept celebrating the arrival of WorldPride in New York City and raising awareness.

Licensing is an important part of our DKNY and Donna Karan business. We recently renewed DKNY's partnership with our watch licensee Fossil. We have a new eyewear licensee Marchon, who showcased their newly designed DKNY eyewear line and launched the product line globally in April. DKNY and Donna Karan offer the opportunity for significant domestic and international growth over the next several years. We've accomplished a lot in a short period of time and have plan to accomplish a great deal more with these two brands.

Overall, spring outerwear performed well for us and we expect that we again will have a good upcoming fall and holiday season. At G-III, we continue to focus on capturing our share of the ever-growing market for online sales, whether it'd be on our own brands, websites of our retail – or our websites of retail customers. Our brands are in demand and we continue to allocate more investments and personnel in the online space.

Lastly, Vilebrequin, our status swimwear and resort brand, had worldwide comparable sales increases in the mid-single digits and continues to do well. This quarter, we opened two new stores, one at the Hudson Yards here in New York City and the second in Sylt, Germany. We continue to focus on selectively expanding the brand brick-and-mortar and digital footprint.

I'll now pass it to Neal for a detailed discussion of our first quarter and our guidance for the second quarter and for fiscal 2020.

Neal S. Nackman

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

Net sales for the first quarter ended April 30, 2019 increased approximately 4% to $634 million from $612 million in the same period last year. Net sales of our wholesale operations segment increased 8% to $571 million from $528 million and Tommy Hilfiger and DKNY brands were the main drivers of this increase. As previously indicated, our growth rate was suppressed by the sales at Bon-Ton in the first quarter of last year.

Net sales of our retail operations segment for the quarter were $82 million, approximately 22% lower compared to last year's sales of $105 million. We reported same-store sales decreases of approximately 23% for our Wilsons stores, 11% for our G. H. Bass stores and 1% for our DKNY stores. Net sales of our retail operations segment were also negatively affected by the decrease of approximately 60 stores operated by us compared to the first quarter of last year.

Our gross margin percentage was 37.3% in the first quarter of fiscal 2020 as compared to 38.3% in the prior year's period. Gross margin percentage in our wholesale operations segment was 34.9% compared to 35.2% in the previous year's quarter. The gross margin percentage in our retail operations segment was 45.2% compared to 46.3% in the prior year's quarter, mostly as a result of higher promotions in the current year to Wilsons stores.

SG&A expenses were flat at $202 million in this fiscal quarter and the same in the previous year. Net income for the quarter of this fiscal year was $12 million or $0.24 per diluted share compared to $10 million or $0.20 per diluted share in last year's quarter.

Non-GAAP net income per diluted share was $0.25 for the quarter compared to $0.22 per share in the prior year. Non-GAAP results exclude the impact of non-cash imputed interest and gain on lease terminations.

Looking at our balance sheet, accounts receivable increased to $478 million from $429 million at the end of the quarter, up approximately 12%, and consistent with our wholesale sales growth. Inventory increased approximately 16% to $539 million. This increase is higher than our forecasted sales growth as a result of accelerated inventory receipts and increases in DKNY inventory, which is still building up and normalizing when compared to launch levels of inventory in the prior year.

In this fiscal year, we adopted Accounting Standards Codification Topic 842 or ASC 842, and additional details regarding the adoption can be found in our first quarter 10-Q, which will be filed with the SEC shortly.

Per ASC 842, we evaluated our portfolio of real estate leases and have accordingly capitalized the lease liability and right-of-use asset associated with these leases on our balance sheet. We expect the impact of applying the new standard to be negligible to our results of operation and cash flows as compared to the previous accounting methods.

We spent approximately $13 million on capital expenditures this quarter. We had long-term debt outstanding of approximately $411 million at the end of this quarter, compared to $448 million at the end of the first quarter last year. In addition, our cash balance at the end of the quarter was $48 million this year compared to $71 million a year ago. We currently have 4.3 million shares outstanding under our authorized share repurchase agreement.

As for our guidance, we are reaffirming our guidance for the fiscal year ending January 31, 2020, and forecasting net sales of approximately $3.28 billion, net income between $163 million and $168 million, or between $3.19 and $3.29 per diluted share. This compares to net sales of $3.08 billion and net income of $138 million, or $2.75 per diluted share in fiscal 2019.

On an adjusted basis, excluding non-cash imputed interest expense of $5.4 million and an $800,000 gain on lease terminations, we are anticipating non-GAAP net income of between $167 million and $172 million, or between $3.25 and $3.35 per diluted share compared to non-GAAP net income of $144 million or $2.86 per diluted share in the previous year. Our guidance continues to assume weighted average diluted share count of approximately 51 million shares.

We're projecting full-year adjusted EBITDA for fiscal 2020 of between $307 million to $313 million, compared to $269 million in fiscal 2019. We now anticipate the non-GAAP retail losses in our retail operations segment in fiscal 2020 will be similar to fiscal 2019. This assumes mid-single-digit comp declines at both Wilsons and Bass for the full year.

For DKNY retail operations, we are planning for a high-single-digit comp increase for the full year. Total sales are planned about flat to prior year for DKNY, as the average comp store count is down. As for DKNY's wholesale and licensing operations, revenues continue to be planned to grow by approximately 20%.

For our second fiscal quarter ending July 31, 2020, we are forecasting net sales of approximately $660 million and net income between $8 million and $13 million, or between $0.15 and $0.25 per diluted share. This compares to net sales of $625 million and net income of $10 million, or $0.20 per diluted share, reported in the second quarter of fiscal 2019.

On an adjusted basis, we are forecasting non-GAAP net income of between $9 million and $14 million or between $0.17 and $0.27 per diluted share, as compared to non-GAAP net income of $11 million or $0.22 per diluted share in the previous year's quarter. And as for our retail operations, we are assuming a mid-single-digit comp decline in total for the quarter.

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. In this difficult geopolitical and retail environment, we continue to have the confidence in our ability to adapt to unique challenges. Anchored on the strength of our global power brands, G-III is poised to achieve significant organic growth over the next several years. Our experience in worldwide sourcing and the size and flexibility of our organization in Asia is a competitive advantage for us.

We remain in a strong financial position, with a healthy balance sheet. I'd like to thank our shareholders, partners and stakeholders for their support.

Thank you, operator. We're now ready to take some questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] And our first question comes from Edward Yruma from KeyBanc Capital Markets. Your line is open.

Edward Yruma
Analyst, KeyBanc Capital Markets, Inc.

Q

Hey. Good morning, guys, and congrats on navigating a very difficult environment. I guess, first, Morris, kind of a bigger picture question. I know you guys have placed a lot of attention on the retail business. You've changed out leadership there. You've closed stores. Yet, as you guys indicated, losses will be comparable year-over-year. I guess, what's your openness to accelerating store closures further or potentially bending the cost curve in a more significant way?

And then as a follow-up, Neal, you guys called out a couple different headwinds to earnings between the tariffs as well as the losses in retail operations, and yet you're able to maintain guidance. I guess, where are you seeing kind of areas of incremental upside versus your plan? Thanks so much.

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

A

Thanks, Ed. Ed, we are very conscious of our problems at retail. We're working hard at mitigating the damage that we have, the damage that possibly we've created. But it takes a while. To snap my fingers and say I am done and take a very aggressive write off is not what I'm ready to do.

We've accelerated our store conversions because we found some exceptional solutions to some of the Wilsons stores. As we had predicted, as we had discussed on earlier calls, as we got DKNY in better shape where we were comfortable with the product, it took a little while, it took three deliveries. And today, we're seeing a dramatic change in performance in our own retail stores as well as the department stores and the European distribution that we have.

We're on track with DKNY and we're finally ready to expand the door count there. We've got short of 40 doors in DKNY today. So the expansion capacity is easily another 60, 70 doors. So we're moving faster than we had originally thought. We've identified several new stores that will be converted into DKNY stores in the coming months.

That said, it takes a little while even to execute that, there's store construction, there's getting the appropriate inventory staged for opening new stores, and with that, we also have picked up traction with Karl Lagerfeld. Karl Lagerfeld is performing exceptionally well. We have one store in Soho that's a non-achiever. It's a very high rent district that we inherited through DKNY. We converted it into Karl Lagerfeld. It's not working, but the good news is the lease is over. We're done with that store at the end of this year. So, that again provides a little aid into prosperity for us.

So, we're on track. And there's nothing that says, I've said before that I can't do anything that's radical. Our balance sheet supports an aggressive write off if needed. I'm not ready to make that call yet. So, we are conscious of it. We're working hard at it. We've changed management, and I think we are on a path to preserve moneys that otherwise would have been written off.

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

A

And Ed, as far as the second part of the question, in terms of the adjustments to the back three quarters, we look at our order book for wholesale and primarily the adjustments that have been positive in terms of top line and bottom line performance are all in the wholesale category across the brands.

Edward Yruma
Analyst, KeyBanc Capital Markets, Inc.

Q

Great. Thanks so much guys.

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

A

Thanks, Ed.

Operator: Our next question comes from Erinn Murphy from Piper Jaffray. Your line is now open.

Erinn E. Murphy
Analyst, Piper Jaffray & Co.

Q

Great. Thanks. Good morning. I guess a couple of questions maybe first starting with the first quarter. As we think about it relative to your expectations that came in at just over $50 million light, retail obviously being a part of that shortfall, but, Morris, if you could share with us what you saw in your non, kind of, five power brand piece of the wholesale business? And then how did Karl Lagerfeld do relative to your expectation?

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

A

So, the non – thank you, Erinn, thanks for your question. The non-power brand business for Q1 is, it's a very small business, quite honestly, so there was negligible impact. The area that we missed a little bit on is our team license business and Kensie which also is – Kensie sportswear, which is not a very important component to our business today or going forward.

All said, we really had what I would term as an excellent first quarter relative to not only the industry, relative to ourselves in the past, our increase in comp sales was north of 8% in wholesale. I'm not sure, I saw many postings that read that way in our universe. So we're pleased. The future couldn't look better. All the experiences of integrating companies, which we're very aggressive on, are behind us. We've got the most amazing talent in this industry, supporting the strategy that we've implemented. They execute well, they execute on an exceptionally timely manner, and the future has never looked better for us.

Erinn E. Murphy
Analyst, Piper Jaffray & Co.

Q

Got it, thank you. And then on tariffs – sorry, yeah.

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

A

I'm sorry. My response to Karl, the only hiccup we have to the original plan, again, it's not our own doing, it's more Lord & Taylor centric than anything else. When we bought the brand, we were very fast to describe what our strategy was. It was going to be a brand that was guided toward Dillard's, Lord & Taylor, The Bay and beyond. It was not a Macy's brand. It was carefully distributed. We never said that this was going to grow quickly, it was going to grow carefully, and it is.

So the only hiccup we're incurring right now is really the unknown future of Lord & Taylor. We're very pleased with the product. When you walk through the showroom, it's a product that makes you smile. It's great quality, it's great design and it's priced affordably. It's a surprise to most consumers as to how affordable it is. It's a brand that really reeks of luxury. We've made it a little bit more moderate and affordable. It's just the brand that we needed.

Erinn E. Murphy
Analyst, Piper Jaffray & Co.

Q

Great. And then just on tariffs, Morris, you talked about price increases that retailers are willing to sharing the burden with. I guess, can you share with us what type of price increases you think you can get through without meaningfully altering kind of consumer demand? And then just mechanically, when would we start to see some of the price increases? And I'm assuming you're just speaking about the handbag side of your business that is currently impacted.

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

A

Sure. There's been a lot of talk on tariff and price increases and moving from country to country. We're yet to hear anybody calculate the damage that could be done in moving at a inappropriate time from one country that's been developed for 30 to 40 years by a vendor and imported, such as ourselves, and being able to do it seamlessly. Our concern is to make a radical move, take out total production out of China. It's very easy. We have a line at our door from factories that we don't do business with, that use the calling card of do business with us and you can avoid tariffs. Well, if we didn't choose to do business with you before, maybe you're not meant for us today.

We're not choosing factories or countries solely on the merit of tariff. We have great product. We worked hard at developing these relationships. We're not very fast to give them up. In a perfect world, there would be – these tariffs wouldn't be in play. But if they are and they become reality, I assure you that we will find a solution. We're not going to abandon 40 years of hard work and quality product for entering into a virgin territory and risking our company. That's not who we are. So, there might be some short-term pain in margin, but I believe this is the best solution for us.

Erinn E. Murphy
Analyst, Piper Jaffray & Co.

Q

Okay, fair. And then just last question for Neal. The inventory, you said you had accelerated receipts which caused the kind of 16% build. It is the highest spread we've seen for several years relative to sales. I'm just curious how do you expect to kind of work that through throughout the year, when should it be more aligned with sales? And was there any kind of pull forward with the accelerated receipts because of tariffs or was it just you guys holding more inventory for retailers? Thank you.

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

A

I think that we've certainly been conscious of the environment as far as trying to take advantage of good pricing as well as potential tariff issues. So, as I mentioned, there were accelerated receipts for both of those reasons, the DKNY business still is in really year two of more maturing and growing. I would tell you that we'd probably still be in a mode of accelerating receipts at the end of the second quarter for sure. And then we would hope that probably by the end of the year that we're probably back in line with – more consistent with future growth.

Erinn E. Murphy
Analyst, Piper Jaffray & Co.

Q

Okay. Thank you, guys. All the best.

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

A

Thank you, Erinn.

Operator: Our next question comes from John Kernan from Cowen. Your line is now open. John Kernan from Cowen, your line is now open.

John Kernan
Analyst, Cowen & Co. LLC

Q

Hey, guys. Sorry about that. Thanks for taking my question. Neal, you took up the order book outlook in wholesale. I'm just wondering if you could share what specific brands, categories, or even channels and partners that are firming up at this point, because we saw a pretty significant deceleration in traffic drop the entire retail ecosystem from January through May. So I'm just wondering where you're seeing maybe better trends play out?

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

A

Yeah. Look, I think that – keep in mind, as Morris mentioned before, we have continued to outperform the marketplace. And what we saw with the order book was really across the brands. I don't have a single item to call out. We had strength across the Calvin brand, Tommy's business, DKNY increases, Karl had a small increase, so they were not extreme.

Our top line sales guide is back to where we were originally. Our miss was significant – was half retail and half wholesale. So we sort of made – certainly made up what was a pretty small miss in terms of the wholesale business. But, no, I don't have any specific brand, product to call out for you, John, other than that.

John Kernan
Analyst, Cowen & Co. LLC

Q

Okay. And then just – Neal, one more for you. Just the confidence in the gross margin reacceleration in the back half of the year. If we look at kind of where Q1 shook out, have some ideas around Q2, and then it does assume some increases in the back half of the year, just given the inventory situation, potential tariff situation in the fourth quarter. Just wondering how – your confidence in that gross margin picture, you do have some pretty – the comparisons for the back half of the year are not typical. But I'm just wondering given the disruption in the retail business and a lot of the uncertainty in the back of the year and inventory being a little elevated, how confident you are in that gross margin outlook? Thank you.

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

A

Starting with the end of your comments, I mean, the inventory increases are not a concern for us. This is not bad inventory; this is good inventory going forward. So we don't see any kind of pressure on margin in terms of cleaning out inventories.

With respect to your accurate view of back half improvement, if you looked at towards the back half of last year, we did have some challenging periods, so the comparison is a little bit easier. If I had to lean into any one particular area, I would tell you that the non-outerwear business in the fourth quarter of last year was probably more impacted by retail selling and some markdown pressure. But that's about it, John. So, we've got it all in our book that that is the basis for our forecasting certainly in the short-term, we're in the mid-70s as far as the order book being completed, which is comparable to where we were last year. And that's what gives us confidence that are – the – with our forecasted figures.

John Kernan
Analyst, Cowen & Co. LLC

Q

Got it. Thank you. And then, Morris, can you remind us the lease expiration timing of the store base? You have been active in reducing the footprint, but I'm just wondering as we look into – beyond fiscal 2020, what the overall store closure cadence looks like?

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

A

I'm going to let Neal respond to that. He'll give it you by year.

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

A

You've got the disclosures in the 10-K. I would tell you that, on average, the retail store base now is down to about a three-year average. I mean, keep in mind that one of the things, we have been extending leases where they make sense and we've been doing that on a short-term basis. So, that's bringing down the average, which is not to say that we don't have some outliers in terms of longer years on some of the stores, but on average, we're making good headway at bringing the lease term down.

John Kernan
Analyst, Cowen & Co. LLC

Q

Got it. And then just last question for me. Donna Karan has been a source of, I think, upside to where you thought it would be. Can you just remind us the margin profile of the business right now as we head into the rest of fiscal 2020?

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

A

Yeah. So, last year, we were low-single digit positive. In the current year, we'll see improvements to that. It's getting a little more difficult to break out the specifics as the business melds in and absorbs different corporate overheads. But, prospectively, just as a reminder, we think that this will be for sure one of the higher operating margins of the business. We're still thinking that that's in the 15% to 20% operating margin range and, again, that's because of the – that's a business that we do not pay royalties on, number one, and, number two, we've got a nice licensing base that's highly profitable for the business.

John Kernan
Analyst, Cowen & Co. LLC

Q

Excellent. Thanks, guys. Best of luck.

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

A

Thanks, John.

Operator: Our next question comes from Rick Patel from Needham & Company. Your line is now open.

Rick B. Patel
Analyst, Needham & Co. LLC

Q

Good morning, guys, and congrats on the new Calvin Klein license. I was hoping you can talk about the opportunity in jeanswear. So, as you look at that line and what it's done historically, what are you most excited about as you think about the opportunity? And along those lines, I was hoping you can touch on the distribution as well, what that looks like in spring 2020 and how quickly you expect to ramp to your $250 million sales target?

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

A

So, basically, let's start with your question on distribution. It's the same distribution as we have in Calvin Klein and Tommy Hilfiger and DKNY. It's a sector of our retail community that we know well, it's not uncharted waters.

As far as where – I'll expand on it a little bit. What we now get is another pad to sit on that is a classification. And we love classifications. That's how we grow our business. It's not a sportswear pad that houses all of what we do. This might be as much as 15 separate locations we would sit in in a Macy's or maybe less so in Dillard's and Lord & Taylor and The Bay and Nordstroms, but it gives us great opportunity.

We're very excited about the denim business. We believe there is – denim is coming back in a very significant way. And we've changed it a little bit from what people would have expected. We are going to be approximately 30% denim and maybe 70% tops. So it's an active area that reads as denim, but it's t-shirts, it's hoodies, it's knits, it's sweaters, it's active outerwear, and it's a change from what's been out there. There's not a retailer that's passed through our showroom, our makeshift showroom, we've not built out a space yet, and has been excited (sic) [has not been excited] about everything that we've done.

It's a lifestyle that has been in existence forever. Denim is an incredibly old fabrication, and we've made it much more modern than one would anticipate. So, distribution is not going to be heavy on the off-price channel. It's priced appropriately. It's exciting, and we believe this is a major growth opportunity for us. I think there's a lot to learn on the way we're marketing this that will transcend into making even Tommy Hilfiger, DKNY and maybe even Karl Lagerfeld a little bit more denim-centric.

Rick B. Patel
Analyst, Needham & Co. LLC

Q

Also a question on retail, so given Wilsons and G. H. Bass are running a bit softer, can you touch on your recently converted stores? Some global brands out there have been talking about tourist headwinds for a while now. So, just curious to what extent that might be affecting your performance in Lagerfeld and DKNY stores?

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

Well, for us, I mean we don't have very much of a comp. What we do have a comp for is Wilsons. Traffic is down. I don't really believe that Wilsons was a major tourist destination. I think that maybe the world can live without a coat outlet store. So, that's more about us than the consumer.

The Bass business, we're retooling on Bass. We're raising our price points. We're delivering better products. And we're seeing a slight difference, traffic would help, but our online business is excellent at Bass and we're picking up. As we get rid of our markdown inventory, there is better effort and better performance on the rest of what we do.

As far as DKNY and Karl Lagerfeld, we believe we are capturing the tourists. I can't tell you we're capturing more or less than last year, because quite honestly I don't believe there was a last year. So this is the first year out as far as I'm concerned with appropriate product, and it's not bad. So, imagine if the tourist was out, how good our business would be.

So we're exactly where we want to be. We have great product. We have great management. And I think we have two great brands that we can build our retail business appropriately with. We never had that. We never had the ability of building out Calvin Klein or Tommy Hilfiger retail. We're a licensee with wholesale rights in North America, and with our own brands, we have the ability of expanding that.

Rick B. Patel
Analyst, Needham & Co. LLC
Q

Thanks very much.

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

Thank you. Thanks for your question.

Operator: Our next question comes from Heather Balsky from Bank of America. Your line is now open.

Heather Balsky
Analyst, Bank of America Merrill Lynch
Q

Hi. Good morning. Thanks for taking my questions. First, I was curious on the Donna Karan and I guess Karl Lagerfeld retail business. The profitability has also been a drag. I'm curious if you can talk about what gets you to better profitability there and even maybe positive operating income?

And then also with regards to your retail business, just curious if 2Q comps are running in line with your guidance for the quarter?

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

So, in response to your question, and I guess what makes us comfortable that we're better at DKNY, I guess I'll paraphrase it. I think I...

Heather Balsky
Analyst, Bank of America Merrill Lynch

Q

Sorry. That would be helpful and also just what gets you to profitability for that retail business?

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

A

I think I've addressed it. I think it's primarily better product, which we have, a product it's taken three deliveries to get it right, which is fine. We are right on the appropriate assortment, the right quality and the appropriate price points for the consumer that we're addressing. So we're seeing a build in our volume in our comp stores. I think that's all about product. I'm not sure it's about tourist. So we're comfortable that we're on a path. Those doors are contributing, their strong contribution to the future of DKNY and Karl Lagerfeld on a four-door basis. And...

Heather Balsky
Analyst, Bank of America Merrill Lynch

Q

And then...

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

A

Oh. And with respect to your second part of your question, I would tell you that the outlet business at present is a little bit under pressure. We certainly have factored that in in terms of the forecast for Q2, but I would tell you that we're off to a little bit of a challenging start in the first month.

Heather Balsky
Analyst, Bank of America Merrill Lynch

Q

Thank you.

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

A

Operator, next question, please?

Operator: Our next question comes from Jim Duffy from Stifel. Your line is now open.

James Vincent Duffy
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Thank you. Good morning. A couple of questions from me. First, Neal, on the SG&A, flat year-to-year in the first quarter. How are you guys doing that and what's the outlook for SG&A for the remainder of the year? Is there an investment in the second half to build towards the launch of the Calvin Klein denim?

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

A

Yeah. So, Jim, the – if you look at the SG&A, we do have less stores. So, on the retail side of our business, we're having decreases in terms of SG&A as a result of the lower store count primarily. The wholesale side, we're really making investments, continuing to make investments as the business grows and those are in the main areas, really people, space and then advertising, more specifically in the DKNY business. So, I would tell you that there is nothing unusual in terms of those increases. We still look for operating margin improvement in the wholesale segment. We'll have a little bit of – hopefully a couple of ticks of both gross margin improvement as well as SG&A leverage throughout the whole year.

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

A

Jim, as it relates to the denim, the increase in or possible increase in the SG&A, as a percentage of sales, we're going to get a great advantage because the areas integrating into our CK Performance area, so leadership will be out of CK Performance. There'll be some additional designers. There'll be some space needs.

And as far as shop build-outs, we have the collaboration with both the retailer and PVH on our need to build out shops in the department stores. So, actually it's a very good asset for us. It's not cost-intensive, I think we have the capability to expand it and expand it rapidly.

James Vincent Duffy
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Great. And then just a question around the environment. I know it's been a challenging spring for softlines. I'm curious, based on what you're seeing today, does an order today mean the same as an order a year ago? Are you seeing cancellations? How do you think about the order book? Is there any movement in whether those orders are firm or more at risk?

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

A

There is nothing that's led me to believe that these orders are any different than in the past. We have a high dependency on some retailers, but conversely, those same retailers have a high dependency on us. We work together. We – more cases than not, a cancellation of product is generally caused by us when we – we have our planners and our analysts evaluating sales from our retailers on a regular basis. And what we don't do is we don't flood inventory into retail stores simply because there is an order in place that is a solid order. We try to mitigate the damage by finding solutions before it's a desperation issue. So there is nothing at all that is – that leads me to believe that an order is any less solid today than it was a year ago, two years ago, five years ago.

The one thing we can't forecast is a surprise bankruptcy. If that occurs, there's nothing I can do about that. But we're exceptionally good on monitoring that. And we work on – and the most amazing awareness factor that you would believe, our network is not only on the frontline in sales, but it's in finance, with communications, with competition, where we're very much aware of what goes on.

Bon-Ton, we were one of the largest suppliers at Bon-Ton, yet we didn't get caught in their bankruptcy, and we were there all the way through the end. I can cite many of these situations, we're careful, we're prudent and we're actually pretty good at what we do on all basis. The organization here is one that I am most proud of, there are lots of changes, but we are rock-solid on the structure.

The structure that cites the impediments of business and deals with them as we've done that historically. And Jim, you've been part of it for many years. You haven't seen too many changes. It's – and this time, I think what you're most happy with when you have an organization like G-III is that you have a vast amount of people that you can depend on to make the right solutions when they appear – when the problem appears. Anyway, little wordy, but I guess it needed to have a call out in these difficult times.

James Vincent Duffy
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Understood and thank you for that. And the last question from me, Morris, can you comment on the opportunity with the off-price channel for the fall season, what does [indiscernible] (51:59-52:06).

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

A

So, Jim, with our licenses, we have a cap, a contractual cap that we're permitted to sell the off-price channel. We're careful with that cap. We don't want to exceed it. We don't believe it's appropriate for the brand. And there's a lineup for our brands, there is basically an allocation that we provide for the off-price channel as to what we will give them in dollar value. So, I can't tell you it's for all our brands, but it is certainly for our, call it, our five power brands. DKNY, where the allocation is created by us, we are very much in sync with licenses that we take from PVH. We try to keep it close to what we have with Tommy and Calvin. So, we don't have an overabundance of product in the off-price channel and we have a very – we always have a high demand for our brands.

James Vincent Duffy
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Great. Thank you.

Operator: And our final question comes from Susan Anderson from B. Riley. Your line is now open.

Luke Hatton
Analyst, B. Riley FBR, Inc.

Q

Good morning. This is Luke Hatton on for Susan. Can you talk about the broader Calvin Klein portfolio performance in the quarter? I think you called out dresses, sportswear and suit as top line drivers, but were there any categories that underperformed relative to your expectations? And then are there any categories also where you're seeing increased space allocation or increased demand from your wholesale partners?

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

A

No, we don't have any specific call-outs other than we – the – just as a reminder, the Bon-Ton business was probably the most significant – the most significant impact of the loss of the Bon-Ton business was on the Calvin Klein brand. So, our volumes were pretty good, we would have had very solid increases in Calvin if you stripped out the Bon-Ton business that we did do with them in the first quarter of last year. And as far as going forward, obviously, it's the Calvin Klein Jeans business is the one that at this point is new space for us that we expect to capitalize very quickly on.

Luke Hatton
Analyst, B. Riley FBR, Inc.

Q

Great. Thank you. And then can you also talk about the growth you're seeing for DKNY at the wholesale partners outside of Macy's and sort of any differences you're seeing in the broader department store portfolio there compared to Macy's?

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

A

Sure. Our business is consistent; it's very good at Macy's. Our shoe business is stellar. Our handbags – little bit difficult time for handbags, but our handbags are right in sync with some of the top-tier handbags that are in the department stores, and it's not only Macy's, it's all the department stores that we sell. And this one we can cite global distribution on where we're doing exceptionally well on footwear and handbags throughout Europe, and we're making inroads on our sportswear, our dresses and our performance apparel.

Some of our franchise partners are opening Performance stores. One has opened two stores and doing incredibly well and planning on expanding the unique concept. So, we're very pleased globally. We don't – we no longer refer domestically to just the Macy's business, although it's our largest account, we've got much broader distribution today and they're all in sync, they're all doing well, trying to create capsule groups that are a little bit different than what we provide to Macy's for some of our other accounts to differentiate them. And it's really on a much stronger platform today than it was a year ago.

Luke Hatton
Analyst, B. Riley FBR, Inc.

Q

Got it. Thanks for taking our questions and good luck next quarter.

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

A

Thank you. Operator?

Operator: That concludes our question-and-answer session.

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

All right. Thank you very much for being with us this morning and talk to you soon. Thank you very much.

Operator: Thank you, ladies and gentlemen. This concludes today's conference. Thank you for your participation. You may now disconnect.